

**REPORTS OF
INCOME TAX CASES
VOL. III**

REPORTS OF
INCOME TAX CASES
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Reprint with a Foreword by

Hon'ble Shri Justice B. MALIK, *M.A., LL.B.*
OF THE HON'BLE SOCIETY OF LINCOLN'S INN., BARRISTER-AT-LAW,
CHIEF JUSTICE, ALLAHABAD HIGH COURT (NOW RETD.)

VOL. III

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REPORTS
OF
INCOME TAX CASES

DECIDED IN
THE HIGH COURTS OF JUDICATURE AND CHIEF COURTS
IN BRITISH INDIA, MYSORE AND TRAVANCORE

EDITED BY
P. R. SRINIVASAN, M.A., B.L.
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VOL. III



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INCOME TAX CASES.

VOL. III.

[224] IN THE HIGH COURT OF JUDICATURE AT CALCUTTA.

Before Sir George Rankin, Kt., Chief Justice, Mr. Justice C. C. Ghose and Mr. Justice Buckland.

[13th December, 1927.]

Gangasagar Ananda Mohan Saha

.. Assessee

The Commissioner of Income-tax, Bengal.

Income-tax Act (XI of 1922), Sec. 66 (2) and (3)—Assessee claiming assessment as undivided Hindu family—Claim rejected and assessment as unregistered firm—Refusal by Commissioner to state a case thereon—Question, if one of law—Duty of Commissioner in stating a case.

The assessee alleging themselves to be members of a Hindu joint family carrying on the family business claimed to be assessed as an undivided Hindu family. This contention being negatived an assessment was made as an unregistered firm and an application for a reference was also rejected by the Commissioner.

On an application under section 66 (3), the High Court directed the Commissioner to state a case on the question whether or not the assessee were entitled to be treated for income-tax purposes as a Hindu undivided family.

In stating a case, it is the duty of the Commissioner to find all such facts as will enable the Court to apply the law and decide the questions referred to it.

The applicants, Messrs. Gangasagar Ananda Mohan Saha, on an assessment to income-tax for the year 1926-27 contended that they were members of a Hindu undivided family carrying on a joint family business and claimed to be assessed as such. This contention was not accepted by the Income-tax authorities who refused to assess the firm as an undivided Hindu family business concern. An application was then preferred to the Commissioner of Income-tax under sections 33 and 66 (2) of the Income-tax Act for revision of the orders of the Income-tax Officer and the Assistant Commissioner and for a reference to the High Court on the following questions of law:

1. Whether the members of a Hindu family, joint in estate and worship, but who have to live in separate mess only for want of accommodation in the original homestead, should be held in law to constitute a joint Hindu family or not?

2. Where the business was started by the members of a joint Hindu family and is confined to the descendants of the original family and no stranger has been taken in and the family is maintained out of the income of their joint estate and business without apportionments thereof amongst the partners, is the family to be regarded for the purpose of assessment as a joint family?

3. Whether non-existence of separate capital account in the names of the proprietors belonging to the same Hindu family and non-allocation of profits among them is conclusive proof or not of undividedness in law?

The Commissioner refused to interfere or make the reference asked for and thereupon an application was made to the High Court under section 66 (3) for directing the Commissioner to state a case on the questions raised above.

Dwaraka Nath Chakravorthy with Gopal Chandra Das and Satyendra Kishore, for the assessee.

Surendranath Guha (Senior Government Pleader) for the Crown.

JUDGMENT.

RANKIN, C.J.—In this case certain assesseees applied to the Court under sub-section (3) of section 66 of the Indian Income-tax Act of 1922 for an order directing the Commissioner of Income-tax to state a case for the opinion of the Court. The application made to the Commissioner of Income-tax appears to have raised in a somewhat complicated and contentious form various questions which apparently include allegations of fact which the Commissioner of Income-tax disputes and which overlap to some extent; but the real question for determination is whether the assesseees are entitled to be treated for income-tax purposes as a Hindu undivided family. The Commissioner of Income-tax is of opinion that they are not so entitled and that they must be treated as an unregistered firm. We direct that the present rule be made absolute on that question, namely, whether or not the assesseees are entitled to be treated for income-tax purposes as a Hindu undivided family. That is the sole question which we require the Commissioner of Income-tax to state for our opinion.

I desire to point out that in these cases it is the duty of the Commissioner of Income-tax to find all the relevant facts. When a case stated comes before this Court, the Court expects to find all such facts stated in the letter of reference as would enable the Court to decide the question referred to it. It is quite true that the Commissioner of Income-tax is required also to give his opinion. He is not merely required to state the questions of law and give his opinion; he is required above all things to state the facts upon which the questions of law must be decided. I trust, therefore, that when this matter comes before the Court again there will be such findings of fact as will enable the Court to apply the law.

The rule is made absolute in the sense which I have stated.

Liberty to amend the petition to put in order.

GHOSE, J.—I agree.

BUCKLAND, J.—I agree.

[225] IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Sir Murray Coutts Trotter, Kt., Chief Justice, Mr. Justice Beasley and Mr. Justice Anantakrishna Ayyar.

[14th December, 1927.]

P. Tiruvengada Mudaliar—

Assessee

The Commissioner of Income-tax, Madras

Referring Officer

Income-tax Act (XI of 1922), Secs. 22 (4), 23 (2), 23 (4), 66 (2) and (3)—Failure to comply with notice after action taken under Sec. 23(2)—

Liability to assessment under Sec. 23(4)—Assessment to the best of judgment—Whether information in possession of the Income-tax Officer to be disclosed to assessee—Application for Reference under Sec. 66 (3)—Question not raised before Commissioner.

At the hearing of this Reference, the counsel for the assessee with the permission of the Court withdrew the Reference which was returned unanswered.

Case [Referred Case No. 3 of 1927] stated under section 66 (3) of the Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

CASE.

In pursuance of the orders quoted above I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (3) of the Indian Income-tax Act, XI of 1922.

2. The facts that led to this reference are as follows:—

The petitioner is the Dubash of Messrs. Volkart Bros., and one of the biggest men in shipping circles in Madras. He controls the entire operations of cargo landing and loading for the "Holland and British India" line and the "Kerr" line and also provisions their steamers. Till the year 1924-25 he was returning annually an income of Rs. 2,700 to Rs. 10,000 from his business and was being assessed on figures varying from Rs. 4,500 to Rs. 16,000. In the year 1925-26 the Income-tax Officer received detailed and trustworthy information about the extent of the petitioner's business which showed that the petitioner had been seriously under-assessed in the past. The Income-tax Officer therefore determined to force the petitioner to disclose his true profits.

For the assessment of the year 1925-26 the petitioner made a return under section 22 (2) of the Income-tax Act, 1922, showing an income of Rs. 29,339 as under:—

	Rs.
Interest on securities	.. 300
Property	.. 17,039
Business	.. 12,000
	—
Total income	.. 29,339
	—

The Income-tax Officer called upon the petitioner under section 23 (2) of the Income-tax Act to adduce evidence in support of his return. After obtaining an adjournment he appeared before the Income-tax Officer on 8th July 1925 and stated that he did not maintain any accounts for his business, that he submitted bills to Messrs. Volkart Bros. for work done for them and that he kept office copies of those bills and would produce such of them as were available on 17th July 1925. He also offered to produce his Mercantile Bank pass book. Mr. Greatorex of the firm of Messrs. Grant and Greatorex appeared for the petitioner on that date and produced the Mercantile Bank pass book. With regard to the copies of the bills submitted to Messrs. Volkart Bros., he said that he would try to get from the firm information regarding the payments made to the petitioner in the year of account and produce it before the Income-tax Officer on 1st August 1925. On 7th August 1925 Mr. Greatorex obtained two weeks time to file the statements. To a reminder issued on 27th

August 1925 Mr. Greatorrex replied by sending a statement giving some brief indication of the method by which Mr. Thiruvengada Mudaliar had arrived at the income of Rs. 12,000 given in the return as having been derived from his business. A copy of the statement is appended—Exhibit A.* With the statement was forwarded a letter from Messrs. Volkart Bros. to the effect “that the sums mentioned by him (Thiruvengada Mudaliar) are more or less in accordance with what we expect him to make.” The Income-tax Officer did not accept this statement as proof of the petitioner’s return and he accordingly wrote to the Solicitors on 5th September 1925 asking when the statements of receipts would be sent. As no immediate reply was received to this letter, the Income-tax Officer issued on 16th September 1925 a notice under section 22 (4) of the Income-tax Act requiring the petitioner to produce on 24th September 1925 at noon the counterfoils of the bills furnished by him to Messrs. Volkart Bros. On 16th September 1925 Mr. Greatorrex replied to the Income-tax Officer’s letter dated 5th September 1925 saying that he had called on the agent of Messrs. Volkart Bros. and had been informed by him that as Volkart Bros. were only agents to the shipping companies they had sent away all the bills, receipts and vouchers for payments made on behalf of the companies and that therefore the bills mentioned in the letter of 5th September 1925 were not available. In response to another request of the Income-tax Officer Mr. Greatorrex also forwarded receipts for certain fixed deposits in the Central Bank of India and the Indian Bank which Mr. Thiruvengada Mudaliar had “by mistake” omitted from his return. On 18th September 1925 Mr. Greatorrex appeared before the Income-tax Officer in another connection and said that the petitioner would not heed his advice and that further communications from the Officer should be addressed to the petitioner direct and not to the Solicitors. The Income-tax Officer understood this statement to mean that the Solicitors, whose conduct in income-tax matters had always been very straightforward and honest, would not represent the petitioner in future. On 19th September 1925 a second notice was issued to the petitioner calling upon him to produce his Indian Bank pass book on 24th September 1925 at noon and on 21st September 1925 a third notice which read as follows:—

“I have already issued to you two notices under section 22 (4), the first on 15—9—25 and the second on 19—9—25. In response to the notice under section 23 (2) you appeared and said that you did not maintain accounts. Having regard to the nature and extent of your business I have every reason to believe that you maintain accounts. Please take notice that unless you produce them on 24—9—25 I will make the assessment under section 23 (4).”

At noon on 24th September 1925 the petitioner was called and was found to be absent. The Income-tax Officer therefore completed the assessment to the best of his judgment under section 23 (4) as under:—

	Rs.
Property	.. 17,039
Business	.. 90,000
Other sources	.. 5,000
	<hr/>
	112,039
	<hr/>

The business income adopted by the Income-tax Officer was based on the information in his possession. After the assessment had been made, a

person representing himself to be Mr. Greator's assistant appeared and asked for an adjournment of the case on the ground that Mr. Greator was out of town. He was informed that the assessment had been completed.

A petition was then put in under section 27. In the course of the proceedings under that section the petitioner was represented by Advocate Mr. Thanikachalam Chettiar, who contended that the petitioner could not be subjected to the penal provisions of section 23 (4) for the non-production of accounts which he did not maintain and that assessment could not be legally made under that section at noon when no hour was specifically mentioned in the third notice calling for the accounts. To satisfy himself whether the petitioner did or did not maintain accounts or could have produced evidence in respect of his income, the Income-tax Officer examined him orally. In the course of the enquiry copies of some of the bills presented by the petitioner to Messrs. Volkart Bros. were produced as also the Indian Bank pass book. On 22nd October 1925 a statement was also filed purporting to show the payments made by Messrs. Volkart Bros. to the petitioner. These payments amounted to Rs. 1,37,376. The evidence produced showed that the bulk of the petitioner's income, *viz.*, that from landing did not reach him through Messrs. Volkart Bros. For landing goods the Dubash receives Rs. 2 per ton from the consignee on dutiable articles and out of that he pays 5 annas to the Port Trust and 6 annas to Messrs. Volkart Bros., leaving him Rs. 1-5-0 which is practically all profit. The copies of the bills for ships' supplies showed that the petitioner must have made enormous profits out of that branch of his business, as the prices charged to the seamen for wholesale supplies were well above the prevailing retail prices. The Indian Bank pass book, which the petitioner did not produce until after the assessment had been made, showed that the petitioner had invested not less than Rs. 60,000 in fixed deposits in various banks, and had lent out about Rs. 14,000. In the course of the examination of the petitioner on oath to which Mr. Thanikachalam Chettiar at first objected, the petitioner attempted to make out that there was no need for him to maintain complete accounts, as all the moneys he received were shown in the books of Messrs. Volkart Bros., and that he could prepare his bills from his cart hire book, his transport book and the manifest book. These books, which according to the petitioner's own admission, contained materials for the computation of his income, had not been produced in response to any of the notices. As the result of his enquiry the Income-tax Officer came to the conclusion that the petitioner had not been prevented by sufficient cause from complying with his notices dated 16th September, 1925, 19th September, 1925 and 21st September, 1925 and accordingly declined to re-open the assessment under section 27. A copy of his order is filed marked Exhibit B.*

An appeal against this order was then filed before the Assistant Commissioner, but nobody appeared on the date of hearing to prosecute it. The Assistant Commissioner did not enter into the question whether regular accounts were or were not maintained but confined himself to the point whether the petitioner was prevented by sufficient cause from responding to the notice dated 16th September, 1925 issued by the Income-tax Officer under section 22 (4) of the Income-tax Act requiring the petitioner to produce before him the counterfoils of the bills furnished by him to Messrs. Volkart Bros. The

Assistant Commissioner held that the petitioner had no sufficient cause for not producing them and dismissed the appeal. A copy of his order under section 31 is filed, marked Exhibit C.*

The petitioner then filed a petition before the Commissioner under section 33 of the Income-tax Act and by a subsequent application under section 66 (2) required him to state a case and refer for the decision of the High Court the following questions:—

“(1) Whether an assessee can be deprived of the right of appeal merely on a contention or the view of the First Income-tax Officer that the assessee must have been maintaining accounts while the assessee contends that he did not maintain accounts, and

(2) whether assessment order could be passed at 12 noon while the hour for production of accounts is not specified and therefore they could have been produced at the last working hour of that day.”

For the reasons stated in his order my predecessor was of opinion that these questions did not arise out of the order of the Assistant Commissioner and refused to refer the questions to the High Court. His order is filed, marked Exhibit D.*

3. The petitioner thereupon moved the High Court under section 66 (3) of the Income-tax Act to direct the Commissioner to refer for its decision the four questions propounded by him in his notice of motion. In its order dated 9th March, 1926 the High Court directed the Commissioner to state a case and refer the following three questions for its decision:—

(1) In case where the assessee contends that he does not maintain account books and the Income-tax Officer is of opinion that the assessee must have maintained accounts, whether such a state of affairs is one which in the absence of any legal evidence to support the Income-tax Officer's opinion justifies an order under section 23 (4) depriving the assessee of the right of appeal.

(2) Whether assessment on any figure is justifiable in the absence of legal evidence without disclosing to the assessee the information upon which the Income-tax Officer may have proceeded and without giving the assessee an opportunity of disproving the correctness of the information received by the taxing officer.

(3) Whether having taken action under section 23 (2) it is competent to the Income-tax Officer to issue notice under section 22 (4) and pass orders under section 23 (4).

4. On receipt of this order my predecessor found that the second and third questions were new questions not raised in the application under section 66 (2). He considered that the petitioner was not entitled in law to raise such questions in an application under section 66 (3). He accordingly moved the High Court for the amendment of the order under Order 47, Rule 1, Civil Procedure Code and Rule 8 of the rules regulating the procedure in respect of applications under section 66 of the Income-tax Act. (Appendix F to the Appellate Side Rules, 1905.) The application was heard on 19th August 1926 by their Lordships Mr. Justice Krishnan, Mr. Justice Ramesam and Mr. Justice Beasley who held that it was not necessary to pass orders on it and that it

THE COMMISSIONER OF INCOME-TAX, MADRAS

was open to the Commissioner to raise a preliminary objection at the hearing of the reference.

5. Before I proceed to give my opinion on the three questions that I have been directed to refer, I respectfully invite their Lordships' attention to this preliminary question, *viz.*, whether the petitioner is entitled to move the High Court for a direction to the Commissioner to refer a question of law which was not raised before him in the course of proceedings under sub-section (2) of section 66 of the Income-tax Act. That sub-section runs as follows:—

“Within one month of the passing of an order under section 31 or section 32 the assessee in respect of whom the order was passed may, by applicationrequire the Commissioner to refer to the High Court any question of law arising out of such order and the Commissioner shall..... draw up a statement of the case and refer it with his own opinion thereon to the High Court.”

In an application under this sub-section the assessee should therefore specify the questions that he desires the Commissioner to refer to the High Court, and if they are questions of law the Commissioner is bound to refer them. But if the Commissioner thinks that these questions do not involve any point of law or that they do not arise out of the order under section 31 or section 32, he may refuse to refer them. It is then open to the assessee to move the High Court under sub-section (3) of section 66 and the High Court may, if it is not satisfied with the correctness of the Commissioner's decision, require him to state a case and to refer to it the questions which the assessee raised before the Commissioner and which in its opinion the Commissioner ought to have referred. Thus it seems to me that the conditions precedent to a motion under sub-section (3) of section 66 are:—

(1) that the assessee has filed an application under section 66 (2),

(2) that he has specified the questions of law which he desired the Commissioner to refer to the High Court, and

(3) that the Commissioner has refused to refer those questions. In the present case the petitioner required my predecessor to refer under section 66 (2) the two questions referred to in paragraph 2 above. My predecessor refused to refer them to the High Court on the ground that they did not arise out of the order under section 31. I venture to think that the only question for consideration by the High Court in a motion under sub-section (3) of section 66 was whether the decision of the Commissioner on the two questions submitted to him by the petitioner was correct. The second and third questions which the High Court has now asked me to refer were not raised before the Commissioner and I venture to submit that they should not be made the subject-matter of decision in this reference.

6. The order of the High Court purports to have been issued not only under section 66 (3) of the Income-tax Act but also under section 45 of the Specific Relief Act, 1877. I am not sure whether the order was really intended to be issued under the latter provision also or whether it merely repeated the heading of the petitioner's application to the High Court. In any case I submit that the petitioner is not entitled to have the above two questions referred to the High Court under section 45 of the Specific Relief Act. An application under that section must,

according to section 46 of the Act, be founded on an affidavit stating, among other matters, the petitioner's demand for justice and the denial thereof. As I have already observed, the petitioner never demanded a reference of these two questions and the Commissioner never refused his request. Further, section 45 of the Specific Relief Act can only be invoked when "the applicant has no other specific and adequate legal remedy" (proviso (d) to the section), and it cannot be said that the remedy provided in section 66 of the Income-tax Act is not specific and adequate. The petitioner has therefore no remedy under the Specific Relief Act.

7. I now proceed to give my opinion on the three questions that I have been directed to refer.

Question (1).—Judging from the nature and extent of the petitioner's business the Income-tax Officer believed that he must be keeping regular accounts to show his transactions and this was put to him in the notice issued on 21st September 1925. The facts stated above abundantly prove that the Income-tax Officer's belief was correct and that the petitioner did maintain accounts to show his receipts from business which he wilfully omitted to produce before the assessment was made. The question does not therefore seem to arise out of the facts of this case. Whatever may be the answer to this question I submit that it will not help the petitioner because the assessment was made under section 23 (4) not only for failure to produce the accounts which the Income-tax Officer believed that the petitioner did maintain, but also for failure to comply with the terms of the other notices issued under section 22 (4) requiring the petitioner to produce copies of the bills furnished by him to Messrs. Volkart Bros., and the Indian Bank pass book, which were admittedly in his possession. In his order on the petitioner's appeal the Assistant Commissioner has held that the petitioner was not prevented by sufficient cause from producing the copies of the bills and this finding of fact has not been challenged by the petitioner. Assessment under section 23 (4) was therefore justified by the petitioner's default in this respect and the assessment cannot be re-opened now whatever opinion may be held on the question under reference.

8. *Question (2).*—The question has been framed in general terms and the answer to it will depend on the sub-section of section 23 under which the assessment is made. Section 22 (2) of the Income-tax Act makes it obligatory on an assessee to make a return of his income when called upon to do so by the Income-tax Officer. If the assessee files a return and the Income-tax Officer accepts it as correct the assessment will be made on the basis of the return under section 23 (1). If however the Income-tax Officer has reason to believe that the return is incorrect or incomplete he must under section 23 (2) of the Income-tax Act require the assessee to produce any evidence on which he may rely in support of his return. If the Income-tax Officer is dissatisfied with the evidence adduced by an assessee, he may call upon him to adduce such other evidence as he may require on specified points. He may also require by a notice under section 22 (4) the production of accounts and documents in the assessee's possession. If the assessee complies with all the notices issued by the Income-tax Officer the assessment must be made "by an order in writing" under section 23 (3). In such a case if the Income-tax Officer decides to reject the evidence and documents produced by the assessee and to base the assessment on some information in his possession, I submit that he

is bound to disclose such information to the assessee and give him an opportunity of rebutting any conclusions that may be drawn from it. If on the other hand the assessee fails to make a return under section 22 (2), or to adduce evidence in support of his return under section 23 (2), or to produce documents and accounts in compliance with a notice under section 22 (4), the Income-tax Officer is required to assess him under section 23 (4) to the best of his judgment, and the assessment so made is not subject to appeal. The only remedy open to the assessee is to satisfy the Income-tax Officer by an application under section 27 that the default was not wilful and to get a fresh assessment made. The assessment in dispute has been made under section 23 (4) and I am of opinion that the Income-tax Officer was not bound to disclose to the petitioner the information on which he based it. The burden of proving his income lies heavily on the assessee in all cases (Evidence Act, section 106), and when an assessee has not merely failed to discharge the burden, but has wilfully refrained from any attempt to do so, there can be no obligation upon the Income-tax Officer to set up a case for criticism. "Random assessments" are a necessary evil in this situation: *Macpherson v. Moore*(1).

9. *Question* (3).—I am of opinion that the Income-tax Officer may issue a notice under section 22 (4) after taking action under section 23 (2) and that, for failure to comply with that notice, he is competent to make an assessment under section 23 (4). Sub-section (4) of section 23 reads as follows:—

"If the principal officer of any company or any other person fails to make a return under sub-section (1) or sub-section (2) of section 22, or fails to comply with all the terms of a notice issued under sub-section (4) of the same section or, having made a return, fails to comply with all the terms of a notice issued under sub-section (2) of this section the Income-tax Officer shall make the assessment to the best of his judgment."

The argument of the petitioner seems to be that the Income-tax Officer can issue a notice under section 22 (4) only when the assessee has not made a return of his income under section 22 (2), and that when once a return has been made he can proceed only under section 23 (2). The use of the phrase "having made a return" in sub-section (4) of section 23 before the words "fails to comply with all the terms of a notice issued under sub-section (2) of this section (section 23)" lends some colour to this argument but I do not think that it is correct. If a notice under section 22 (4) could be issued only when a return has not been filed, it would not have been necessary to mention the failure to comply with that notice as one of the grounds for making an assessment under section 23 (4), because the assessment has to be made under that section owing to the prior failure to make a return and the non-compliance with a notice under section 22 (4) will not affect the method of assessment. The only condition imposed by section 22 (4) upon the issue of a notice under that section is that a notice under section 22 (2) must have been served on the assessee. It follows that a notice under section 22 (4) may be issued at any time before the assessment is made, whether the assessee has made a return of his income or not. When a return has been made the Income-tax Officer has to issue a notice under section 23 (2) giving the assessee an opportunity of proving his return by the production of such evidence as he chooses. This

(1) 6 Tax Cas. 114.

does not, however, deprive the Income-tax Officer of his right to require by a notice under section 22 (4) the production of specific accounts and documents in the assessee's possession which, he considers, would help in making a correct assessment. If the assessee withholds these accounts and documents he is liable to be assessed under section 23 (4).

Nugent Grant and O. Thanikachalam Chetti, for the assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

The assessee requesting permission this day to withdraw the reference, it is ordered that the assessee be and hereby is given permission to withdraw this reference; and it is further ordered that the assessee do pay to the Referring Officer the Commissioner of Income-tax, Madras, Rs. 150 for his costs in this case.

[226] IN THE HIGH COURT OF JUDICATURE AT RANGOON.

Before Mr. Justice Cunliffe and Mr. Justice Carr.

[3rd January, 1928.]

Rao Bahadur S. Ramanatha Reddiar

Assessee

The Commissioner of Income-tax, Burma.

Income-tax Act (XI of 1922), sections 10 (2) (vi) and (ix) and 66 (2)—Assessee owning fleet of cargo boats—Claim for alleged expenditure on repairs—Rejection of claim, as accounts not kept satisfactorily—Disallowance of depreciation as prime cost not furnished by assessee—Questions, if raising points of law for reference—Limitation period for application to Commissioner under section 66 (2)—Bare appellate order without reasons or grounds therefor given to assessee—Computation of the period.

The assessee, owner of a fleet of cargo boats, claimed an allowance of the sum of Rs. 1,16,989 as amounts expended on repairs to his vessels in the account year and also the allowance for depreciation on the total value of the fleet under section 10 (2) (vi) of the Act. A moiety of the claim for repairs was rejected on the ground that from the accounts kept by the assessee it was not possible to differentiate capital from current payment or allocate individually items of expenditure on repairs to individual vessels. The depreciation claim was disallowed in the absence of information as to prime cost and of the capital accounts. On the dismissal of an application to the Commissioner under section 66 (2) for a reference on six questions of law alleged to arise out of the orders rejecting the claims, the assessee applied to the High Court under section 66 (3) of the Income-tax Act and section 45 of the Specific Relief Act.

Held, in dismissing the application, that the question whether expenditure in a shipowner's business was current as opposed to capital expenditure was essentially one of degree and therefore one of fact and that the computation of the deduction for wear and tear in the absence of the prime cost or the capital accounts was also one of fact.

A decision on questions of fact must always be considered by an Appellate Court from the point of view whether although the decision is indubitably one of fact, there was sufficient evidence to come to a proper conclusion.

If a decision of fact is founded upon insufficient evidence, a question of law is produced which may be considered by any Court of Appeal.

Smith *v.* The Incorporated Council of Law Reporting, 6 Tax Cas. 477; Usher's Wiltshire Brewery *v.* Bruce, 6 Tax Cas. 399; Currie *v.* The Inland Revenue Commissioners, 12 Tax Cas. 245; Cecil *v.* The Inland Revenue Commissioners, 36 T.L.R. 164; referred to.

Where the bare result of an order dated 27th May, 1926 dismissing an appeal under section 31 of the Income-tax Act was communicated to the assessee on 1st June, 1926, and on his application made on 12th June, the actual order containing the reasons was furnished to him on 26th June.

Held, that an application to the Commissioner under section 66 (2) of the Act made on 3rd July was not barred, the intention of the Legislature in prescribing the 30 days limitation period being that the appellate authority should communicate his reasons to the assessee at the same time as his bare decision.

Obiter.—It will not be open to the Commissioner to waive the statutory period prescribed for an application under section 66 (2) of the Act.

Application [Civil Miscellaneous Application No. 71 of 1927] under section 66 (3) of the Indian Income-tax Act (XI of 1922) and section 45 of the Specific Relief Act (I of 1877) for an order directing the Commissioner of Income-tax, Burma, to state a case for the opinion of the High Court.

Foucar, for the applicant.

A. Eggar (G.A.) for the respondent.

JUDGMENT.

CUNLIFFE, J.—This is an application for a rule to obtain a mandamus under section 66 (3) of the Indian Income-tax Act, 1922. In the alternative, by an amendment, the application is made under section 45 of the Specific Relief Act. The applicant is one Rao Bahadur Ramanatha Reddiar. He seeks to direct the mandamus against the Commissioner of Income-tax, Rangoon, and the Government Advocate appears on the Commissioner's behalf to show cause against the rule.

On the 28th of May 1925, an order was passed by the Income-tax Officer, Rangoon, assessing the applicant for the year 1923-24 on an income of Rs. 2,16,833. The applicant appealed from this order to the Deputy Commissioner of Income-tax, who on the 27th May 1926 rejected the appeal. On rejection, the applicant applied to the Commissioner of Income-tax to refer to this Court six questions of law alleged to arise out of the order of the Deputy Commissioner. This application was made under the provisions of section 66 (2) of the Income-tax Act aforesaid. The Commissioner, however, in an order dated the 19th of March 1927 rejected the application. He took the view that the six questions of law put forward by the applicant did not arise, as in his opinion the six questions were not questions of law, but were questions of fact. It is with the object of making the Commissioner alter his opinion in this respect that the present application to obtain a rule is presented.

Section 66 (2) of the Indian Income-tax Act is in these terms:—

“Within one month of the passing of an order under section 31 or section 32, the assessee in respect of whom the order was passed may, by application accompanied by a fee of one hundred rupees or such lesser sum as may be prescribed, require the Commissioner to refer to the High Court any question of law arising out of such order, and the Commissioner shall, within one

month of the receipt of such application, draw up a statement of the case and refer it with his own opinion thereon to the High Court."

Section 66 (3) runs as follows:—

"If, on any application being made under sub-section (2), the Commissioner refuses to state the case on the ground that no question of law arises, the assessee may (within six months from the date on which he is served with the notice of refusal) apply to the High Court, and the High Court, if it is not satisfied of the correctness of the Commissioner's decision, may require the Commissioner to state the case and to refer it, and on receipt of such requisition, the Commissioner shall state and refer the case accordingly."

The first objection taken by the Crown to the application is that it is out of time. The order of the Assistant Commissioner made under section 31 of the Act disposing of the case on appeal is dated the 27th May 1926. The application to refer the points of law was not made until the 3rd of July, 1926.

The first answer to the Crown's objection is that the Commissioner himself waived the irregularity by considering the application and refusing to accede to it. I am of opinion, however, that it is not open to an executive officer to waive a provision of a statutory enactment in such a manner.

The second answer to the contention is a more substantial one. By an affidavit sworn on the 6th August 1927, (to which there is no answering affidavit), the applicant himself deposes that he did not obtain a copy of the Deputy Commissioner's order dismissing the appeal in time to allow his advisers to formulate the questions of law said to arise. In fact, the bare result of the order was communicated to the applicant on the 1st of June 1926. An application to obtain the reasons supporting the order was made on the 12th, but the actual order containing the reasons was not furnished to the applicant until the 26th of June 1926. This is admitted by the Crown. It seems to me that when the Legislature allowed 30 days to the subject in which to make an appeal, it never intended that the Deputy Commissioner should not communicate his reasons to the assessee at the same time as his bare decision. It is manifestly impossible for any person to make up his mind whether a point of law arises unless he has proper materials to do so, before him. The mere statement that his appeal has been allowed or dismissed is not sufficient. It has often been said that the Revenue Statutes should be construed in favour of the subject. In my view, it is much more important in this connection that any rights of appeal contained in Revenue Legislation be strictly construed as to their exact meaning as far as they allow specific time in which an effective appeal can be put forward. It can easily be seen that a glut of work in the Office of a busy Commissioner might completely deprive an assessee of his right to appeal at all. Such a state of affairs would not be carrying out the intention of the statute, and in this case, therefore, although I think that no conduct of the assessee himself could have enlarged to his advantage the statutory period under the section, neither can any conduct of the executive diminish the full period of time allowed to reflect upon and decide whether action should be taken by way of approach to this Court.

There is a still further contention, however, on the part of the Crown which remains to be discussed. The contention is this: that the consideration by the Commissioner of the points of law put up by the applicant was not done at the instance of the applicant at all, but was

carried out *suo moti*: under the provisions of section 33 of the Act. It is not difficult to see why this attitude is now adopted, because if action was indeed taken under section 33, no application could be made to this Court under section 66 (3). The manner, however, in which the Commissioner dealt with his order of the 21st of August, 1926, his heading the order as an appeal and his recital and discussion of the exact questions proposed to him by the applicant and now before this Court, appear to me to negative the contention that the Commissioner proceeded under section 33 alone. It seems to me that had the Commissioner taken this view at the time, he must have notified the assessee or his advisers of the special course he was taking and of the section under which he proposed to proceed.

For these reasons, in the circumstances of the case I am of opinion that the applicant cannot be deprived of his rights of appeal under section 66 (3) of the Act.

On a perusal of the order made by the Income-tax Officer, of the order by the Deputy Commissioner dismissing the appeal and of the order made by the Commissioner himself, it is to be noted that there are two main points in dispute between the assessee and the Income-tax Officials. The first point is in relation to the amount to be allowed for repairs to the vessels of the cargo fleet compared with the amount claimed. The second point is in relation to the depreciation of the total value of the fleet.

The attitude taken up by the Income-tax Officer, with regard to the claim for the amount expended on repairs, which is put forward by the assessee at the figure of Rs. 1,16,989, was to disallow Rs. 58,500 of the claim under this item. The Income-tax Officer thought that the claim under this heading was exaggerated and in fact untrue. He found definitely that the figure Rs. 1,16,989 did not represent current repairs only, but also included replacements on individual vessels, which amounted not to expenditure made for the purpose of earning on the existing vessels, but to a capital expenditure, which the Act under section 10 does not allow to be deducted for income-tax purposes. The reason given by the Income-tax Officer for coming to this conclusion is that he was unable to allocate individual items of expenditure on repairs to individual vessels. This was owing to the manner in which the assessee has kept his accounts. The Income-tax Officer's view of the claim in relation to repair expenditure was shared on appeal by the Deputy Commissioner. The Deputy Commissioner also thought that the amount allowed for current repairs as opposed to capital expenditure was fair and reasonable. He thought that the material by way of accounts which was afforded by the assessee to the Department was slender and unsatisfactory and could give no proper guide to a division between the two forms of capital and current payments. He was of the opinion that the assessee could, if he chose to do so, produce vouchers and pay rolls to support the accounts put forward and to explain them without any ambiguity. When the matter was considered by the Commissioner he took the same view as his two assistants, but perhaps a little more strongly. He was of the opinion that there was a deliberate attempt on the part of the assessee to conceal the nature of the expenditure on his fleet. He found that the expenses for repairs to the shipping, for example, were deliberately included in the accounts of a saw mill owned by the assessee. The Commissioner sets forth in his order that the history of the dealing between the Department and the assessee in the past has been far from satisfactory. The Commissioner said

that prior to the assessment of 1921-22, although accounts were admittedly in existence, none were ever produced. It was not until the assessment of 1921-22 that accounts were put forward. In these accounts in the category of repairs, a large item was included which was subsequently admitted to have been spent on the construction of new vessels. Having regard to this previous history the Commissioner came to the conclusion that where the Income-tax Officer is dissatisfied with the materials produced to support a claim, he is entitled to draw the inference that the claim ought to be partly disallowed. Finally the Commissioner asserts that such an inference is an inference of fact alone.

As to depreciation, the attitude taken up by the Income-tax Officials (and they all share the same view) is that there were no proper materials before them to deal with the question of depreciation at all. It is contended by the Department that the only basis on which a claim for depreciation can be computed is prime cost of the property which is said to have depreciated. It is mentioned in the order of the Deputy Commissioner that the requirements of the Department in respect of depreciation allowance have been frequently and fully explained both to the assessee and to his advisers; in spite of these, no capital accounts, it is said, have ever been put forward in relation to the business and therefore there are no accurate materials upon which the correct capital value of the fleet can be ascertained. Nevertheless what appears to be an *ex gratia* depreciation allowance of Rs. 15,000 was eventually ordered by the Commissioner.

The six alleged questions of law are as follows:—

(a) If in a case where certain sums have been shown as expended on repairs, is it open to the Income-tax authorities to hold that some part of the said expenditure is capital expenditure, having regard to the fact that the business in which the expenditure is incurred is that of a cargo boat-owner and it is not asserted by the Income-tax authorities that any additions or alterations have been made to the cargo boat fleet, or that any specific capital expenditure has been made?

(b) Whether in law a finding that a certain part of admitted expenditure is capital expenditure is maintainable without any finding as to the precise manner in which the said expenditure became capital expenditure?

(c) Whether in view of the fact that petitioner's business was in existence long prior to the year 1922, when the present Income-tax Act came into force, it is maintainable that before any allowance for depreciation can be made, it is essential that petitioner should supply particulars of the prime cost of his fleet?

(d) If the assessee is unable to supply full particulars of the prime cost of his fleet, is he to be debarred from claiming any allowance for depreciation on any other basis whatsoever?

(e) Where, as in the case of the petitioner, the business is an inherited one, in what manner is the prime cost of plant, machinery, etc., to be ascertained?

(f) Whether the petitioner is debarred, under the circumstances of the present case, from maintaining and establishing any claim for depreciation?

Sub-sections (1) and (2) of section 10 of the Indian Income-tax Act run as follows:—

"(1) The tax shall be payable by an assessee under the head 'Business' in respect of the profits or gains of any business carried on by him.

(2) Such profits or gains shall be computed after making the following allowances:"

Sub-paragraph (V) of section 10 referring to allowance is as follows:—

"(V) In respect of current repairs to such buildings, machinery, plant or furniture, the amount paid on account thereof."

The vessels of the cargo fleet owned by the present assessee are, *qua* that part of his business, his plant. They have been so treated by the Income-tax people.

The question whether a point of law arises on any given finding, or whether in reality the alleged point of law is merely a conclusion of fact appears to be a somewhat difficult one depending to a great extent on the particular circumstances of each case. There is no doubt that in the earlier history of the construction of statutes relating to income-tax, a great many questions were considered by the Courts as questions of law which were in reality questions of fact. But when the exact meaning of the various definitive terms contained in the sections become gradually settled and the principles of taxation well established, we find a much more distinct line drawn between law and fact. The leading cases on the different English Revenue Statutes deal with principles cognate to those which govern the Indian legislation and the following pronouncements by English Judges appear to me to be particularly cogent to the elucidation of the first broad question. In the case of *Smith v. The Incorporated Council of Law Reporting for England and Wales* (1) Lord Justice Scrutton (then Mr. Justice Scrutton) dealt with a similar question of principle which arose in considering a case stated by the Commissioners of Income-tax for the Division of Lincoln's Inn. The Commissioners had found that a certain gratuity made by the Council of Law Reporting to one of their reporting staff on his retirement after a long service was allowable to the Council as a business expense in calculating their profits on the year for income-tax purposes. The Crown appealed arguing that the question whether such a payment could be deducted from the Council's profits as being money wholly and exclusively laid out or expended for the purpose of their business within the meaning of Schedule D of the English Income-tax Act was a question of law and not of fact. Lord Justice Scrutton disagreed with this view and on page 684 says this: "It seems to me that the question whether money is wholly and exclusively laid out or expended for the purposes of trade is a question of fact." Later on in the judgment the learned Lord Justice went on to say that in many cases the question whether the money was wholly or exclusively laid out or expended for the purposes of trade must depend upon a knowledge of the facts of the trade, of the way in which it is carried on, and of the effect of payments made in that trade, all of which are questions of fact.

This interpretation was shared by the House of Lords in deciding a very similar question. In a judgment delivered by Lord Sumner in the case of *Usher's Wiltshire Brewery v. Bruce* (2) where a finding of the Court of Appeal delivered by Sir Samuel Evans, in which he stated that "when the various circumstances and facts upon which the question depends are established

(1) 6 Tax Cas. 477; (1914) 3 K.B.D. 674.

(2) 6 Tax Cas. 399; (1915) A.C. 433.

and found, the proper inference in order to determine whether payments were wholly and exclusively laid out for the purposes of the trade or concern within the meaning of the provisions referred to is a question of law", was reversed, Lord Sumner said that the judgment appealed against really found facts and did not, as Sir Samuel Evans thought it did, rule the law when it declared that the rents foregone were losses of an annual value and not expenses of the trade. Lord Sumner added: "Though the answer to the question may itself be an inference from a wide area of facts, it is an answer of fact. There is no suggestion here that the Commissioners found the facts under any mistake in law including in that term the view, conscious or unconscious, that a fact may be found although there is no relevant evidence to support it."

So too, in the case of *Currie v. The Inland Revenue Commissioners*(3), Lord Sterndale decided a question which in my opinion is very similar in principle to the question raised here. In that case the point turned on whether a particular person carried on a profession within exception (c) of section 39 of the English Finance Act No. 2 of 1915, so as to exempt him from assessment to Excess Profit duties. Lord Sterndale thought that whether a person carries on a profession, or whether he carries on a business or trade was essentially a question of fact to be determined by the Special Commissioners of Income-tax alone. Lord Justice Scrutton, who also delivered a judgment in the case, referred to the decision in *Cecil v. Inland Revenue Commissioner*(4) where Mr. Justice Rowlatt had taken the same view in determining the exact status of a photographer. Commenting upon Mr. Justice Rowlatt's Judgment and agreeing with it, Lord Justice Scrutton said: "Art is a matter of degree, and to determine whether an artist is a professional man depends in my view on the degree of artistic work that he is doing. All these cases which involve questions of degree seem to me to be eminently questions of fact which the Legislature has thought fit to entrust to the Commissioners who have, at any rate from their very varied experience, at least as much knowledge, if not considerably more, of the various modes of carrying on trade than any Judge on the Bench."

Applying then the principles enunciated above I am of opinion that the question whether expenditure in a shipowner's business is current as opposed to capital must essentially be one of degree and therefore one of fact. To elucidate the problem in this particular case there were no doubt in addition to the material provided by the assessee a number of outside considerations which actuated the minds of the Officials of the Department, such as their knowledge of the conditions in the port of Rangoon, of the ordinary life of this particular type of wooden cargo boat and of the standard of cost an owner such as the present applicant might be likely to adopt in keeping his vessels in serviceable condition. A decision on questions of fact, however, must always be considered by an Appellate Court from the point of view whether although the decision is indubitably one of fact, there was sufficient evidence to come to a proper conclusion. If a decision of fact is founded upon insufficient evidence a question of law is produced which may be considered by any Court of Appeal. In this particular case there may have been imperfect material on which to found a

(3) 12 Tax Cas. 245; (1921) 2 K.B. 332.

(4) 36 Times Law Report 164.

conclusion, but such lack of evidence and insufficient material was, in my opinion, due to the neglect of the assessee and therefore its insufficiency cannot be used to throw over the question of fact a cloak of law. No one can take advantage of his own negligence, otherwise a wilful non-compliance with the Act might place an assessee, temporarily at any rate, in a most advantageous position. I, therefore, think that the whole question of the expenditure upon these cargo vessels is a question of fact to be determined by the Income-tax Officials alone.

On the question of depreciation, I have little difficulty in deciding against the applicant. The exact amount of depreciation of any plant within a given period is also a question of degree and therefore a question of fact, see *The Peninsular and Oriental Co. v. Leslie*.⁽⁵⁾ Allowances for depreciation are dealt with under section 10, sub-section (2), sub-paragraph (6) of the Act; but it is a condition precedent to obtain any allowance under this heading that the particulars prescribed by the Act should be furnished to the Income-tax Officer. A form is prescribed which includes capital expenditure and we know from the order of the Commissioner that no capital accounts have ever been disclosed by the assessee. From the very wording of the proposed questions before the Court the assessee shares this view. *Ex concessio*, therefore, there was no sufficient material before the Commissioner. It is impossible to decide any question on an allowance of depreciation unless the statement of the prime cost is in the hands of the Income-tax Commissioner. Depreciation allowances are on a percentage basis and therefore the prime cost is essential. I am further of the opinion that it is no part of the duty of the Court to advise the assessee how he ought to keep his accounts, or how to satisfy the Income-tax Officer over his method of accounting. It is impossible for the purpose to compute any deduction for wear and tear without proper material and therefore the question of this deduction is also in the circumstances I find, a question of fact. Nor can I hold that the Income-tax Officials have behaved at all unreasonably in this regard.

For these reasons, I am of opinion that the alleged questions of law are not questions of law but questions of fact for the Commissioner of Income-tax alone. It is therefore not necessary for me to consider any question under section 45 of the Specific Relief Act. Accordingly the rule will be discharged as not coming within the provisions of section 66 (3) of the Income-tax Act of 1922.

Costs in favour of the Crown will be allowed at fifteen gold mohurs.
CARR, J.—I agree.

[227] IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Justice Sir Cecil Walsh, Kt., K.C. and Mr. Justice Banerji.

[4th January, 1928.]

Chandra Sen Jaini, Vaid, Etawah

v.

.. Assessee *

The Commissioner of Income-tax, United Provinces

.. Referring Officer.

Income-tax Act (XI of 1922), Secs. 22 (2), (4), 23 (3) and (4)—Assessee sending in a return of income—Subsequent issue of a combined notice under

* (1928) I.L.R. 50 All. 589; 26 A.L.J. 340; A.I.R. (1928) All. 283.
5. (1900) 4 Tax Cas. 177.

Secs. 22 (4) and 23 (2) to produce accounts and evidence—Non-production of accounts by assessee—Assessment under Sec. 23 (4), if legal—Jurisdiction to issue notice under Sec. 22 (4) after return.

If an assessee made a return in compliance with a notice under section 22 (2) of the Income-tax Act and thereafter a notice was served upon him under section 22 (4) and he failed to comply with that notice, the Income-tax Officer is entitled to make an assessment under section 23 (4) and is not bound to proceed under section 23 (3).

Brijraj Ranglal v. Commissioner of Income-tax, Bihar and Orissa, 2 I.T.C. 458, Dissented from.

Case [Miscellaneous Case No. 1027 of 1927] stated under section 66 (2) of the Income-tax Act (XI of 1922) by the Commissioner of Income-tax, United Provinces, for the opinion of the High Court.

CASE.

1. Lala Chandra Sen Jaini, a *Vaid* of Etawah, duly filed his return of income for the current year, stating his income to have been Rs. 300 from property and Rs. 3,000 from business, and adding that he kept no accounts, that his business was that of a *Vaid*, that he could not complete the form in detail, and that his return was an estimate.

2. When the Income-tax Officer came to make the assessment, he issued a combined notice under section 22 (4) and section 23 (2) of the Income-tax Act in the form attached asking Lala Chandra Sen Jaini (i) to produce or cause to be produced his account books for the previous year, and (ii) to produce or cause to be produced evidence in support of his return.

3. The assessee appeared before the Income-tax Officer and stated on oath that he had no accounts or *bahi khatas* of any sort whatsoever, but on being questioned admitted that he did maintain a register in which were recorded the names of the persons to whom parcels were sent by post value payable and also the amounts of money so realized. The Income-tax Officer asked the assessee to produce that register no matter what its condition was but the assessee declined to do so. The Income-tax Officer accordingly framed an assessment under section 23 (4) of the Income-tax Act.

4. The assessee subsequently presented an application under section 27 in the following terms:—

“Respectfully it is submitted that the applicant was required to file his account books, but since he kept no regular account books he could not file any. The applicant has been assessed to pay Rs. 904-1-1 which is very excessive. The applicant does not sell any medicines in the city. All his medicines are sent outside by means of parcels. A parcel journal is kept by the applicant, which will show the total amount of medicines sold by him.

“The applicant never thought that this journal could afford a reasonable basis for assessment, but his legal advisers have advised him to file this journal. This journal contains all the sales by the applicant, and, by taking average profits per cent, a fairly accurate income of the applicant can be obtained.

“It is therefore prayed that the Court be pleased to reconsider the case in the light of the parcel journal and to assess the applicant accordingly.”

The Income-tax Officer held that the condition postulated in section 27 was not fulfilled, i.e., that the assessee had not been prevented by sufficient cause from complying with the notice under section 22 (4), and rejected the petition.

5. The assessee appealed to the Assistant Commissioner of Income-tax, who rejected the appeal on August 11, 1927.

6. About this time a case in *Brijraj Ranglal v. Commissioner of Income-tax, Bihar and Orissa* (1) was decided by the Patna High Court which ruled that the notice under section 22 (4) of the Income-tax Act can only be issued before a return of income is filed and that failure to produce accounts in response to a notice issued after submission of a return does not render the assessee liable to an assessment under section 23 (4). The assessee noticed a report of this case in the newspapers of August 13, 1927, and has presented a petition claiming that the assessment should have been made under section 23 (3) and not section 23 (4), and praying the Commissioner to set aside the assessment, or to state a case to the High Court. Strictly speaking, the demand for a reference does not arise out of the appellate order. But the matter is of importance and although the judgment of the Patna High Court has no force in this province, it is desirable that the point should be settled authoritatively.

7. The Commissioner, therefore, states a case on the following point:

If an assessee has made a return in compliance with a notice under section 22 (2) of the Indian Income-tax Act, 1922, and thereafter a notice has been served upon him under section 22 (4) and the assessee has failed to comply with that notice, is the Income-tax Officer entitled to make an assessment under section 23 (4) on account of that failure, or is he bound to proceed under section 23 (3)?

8. The Commissioner is of opinion that the ruling of the Patna High Court is not correct and the answer to the first part of the question is in the affirmative, and to the second part in the negative.

FORM B.

Notice under section 23, sub-section (2) (and section 22, sub-section (4) of the Indian Income-tax Act, (XI of 1922).

(For use where a return has been made.)

No.

Dated the

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To

To enable me to test the correctness of the return of your income furnished by you under section 22, sub-section (2) of the Act for the year ending

I hereby require you to attend at my office at

on in person or by representative and to produce or cause to be produced at the said place and time the accounts and documents specified overleaf* and any other evidence on which you may rely in support of the return.

1. 2 I.T.C. 458.

*Particulars of accounts and documents.

Wilful failure to comply with this notice will entail the forfeiture of your right of appeal under section 30 (1) of the Act and will render you liable to prosecution under section 51, sub-section (d) of the Act.

Income-tax Officer.

Baishwari Prasad, for the assessee.

Uma Shankar Bajpai, for the Crown.

JUDGMENT.

WALSH, J.—This is a case stated by the Income-tax Commissioner. The assessee, one Lala Chandra Sen Jaini, a *vaid* or physician of Etawah, filed a return of his income for the current year stating that he kept no accounts and that his return was an estimate. The Income-tax Officer, presumably having reason to think that the assessee was not giving that attention to his return which, we hope, he gives to his patients, served a double notice upon him, one under section 22 (4) requiring him to produce accounts and documents in support of his return, and another under section 23 (2) requiring him either to attend or to produce evidence in support of his return. The notice issued is headed "Form B". It is a double form calling upon the assessee to do two things, to produce documents to enable the correctness of the return to be tested and to attend and give any evidence the assessee may desire to give. This double form, which is a useful and practical way of combining two stages into one, is headed "Form B". We have been unable to ascertain, either from the Manual in use in these provinces, or from the gentlemen who have argued the case before us, whether it is a statutory form or merely a form with no greater authority than that of the department from which it issues. But it is not without significance that one of its sub-titles is in the following terms: "For use where a return has been made." The question whether a double form like this, and the practice of combining two stages into one is strictly lawful, is not before us. It certainly ought to be. It must be a great saving of time to an assessee, especially if he is honest and wants to be truly assessed and to pay the proper proportion of his contribution to public funds, and it must also be of great advantage to the taxing authorities to have one comprehensive and final stage of enquiry where an assessee, whose return has been challenged, can produce all his documents in support of his return and give any evidence on which he relies. The assessee complied with the notice which required him to attend under section 23, presumably because he was advised that if he did not, he would have the very assessment made against him of which he complains, but he did not comply with the part of the notice requiring him to produce his documents, apparently relying upon an authority of the Patna High Court, which he was advised would enable him to withhold them from the taxing authorities. But the result of his attendance to give evidence was to show that his statement in his original return was a falsehood. He had said that he kept no accounts. He did. When he was put upon oath, he admitted that he kept a register with the names of his customers and the amounts realized. He made the feeble and obviously dishonest excuse that he had not produced the register because the accounts were not clearly entered. It is to be observed that he was not called upon to produce accounts which were clearly entered, or anything which he might, as the sole judge of the matter, consider worthy of being produced, but he was called upon to produce such accounts and documents as he had, and it being immaterial whether the accounts were clear or not or whether they were, what is considered, regular and perfectly

kept accounts; he finally said that he did not wish to produce them. He was thereupon assessed by the Income-tax Officer to the best of his judgment under section 23 (4). The question is whether the Income-tax Officer had jurisdiction to do that. It seems to us that if he had not, the careful provisions of sections 22 and 23, for the purpose of preventing fraud and concealment, would be useless and that the machinery provided for the purpose of making people pay their real quota, would break down. The machinery provided by these sections for extracting a reasonable contribution out of assessee in default, is aimed precisely at the conduct of which this assessee has been guilty, but we have to see whether his dishonest attempts to evade his liability are protected by the law. The sub-section in question is 23 (4): 'If the principal officer of any Company, or any other person fails to make a return under sub-section (1) or sub-section (2) of section 22, as the case may be, or fails to comply with all the terms of a notice issued under sub-section (4) of the same section or, having made a return, fails to comply with all the terms of a notice, issued under sub-section (2) of this section, the Income-tax Officer shall make the assessment to the best of his judgment.'

That sub-section contemplates three contingencies. The first, the failure to make a return at all. The second, the failure to comply with a notice requiring production of accounts or documents required by the Income-tax Officer, and third, the failure to attend at the Income-tax Officer's Office, or to produce evidence on which the assessee relies. In each of these three cases the assessee is a person in default, and he can only become in default by a deliberate breach of an express provision to which the penal section which we have just cited in each case refers. It must be admitted that the assessee in this case failed to comply with the terms of the notice issued under sub-section (4) of section 22, because he failed to produce this register which was the important document which he had. By a curiously tortuous form of argument it is suggested that this default on his part does not bring into operation section 23, sub-section (4), because it does not constitute a breach of sub-section (4) of section 22. For the purpose of that argument it is necessary to introduce into section 22 (4) an express or implied provision that a notice requiring an assessee to produce accounts and documents can only be served before he has made a return, and if served after he has made a return, is illegal. To our minds this is a far-fetched suggestion, but as it has been accepted in one High Court in India and is relied upon in this case, it is necessary to examine it with some care. It is impossible to deny that the effect of such an interpretation is to make a great part of these sections unworkable, and the view seems to us completely out of touch with the realities of the question to be determined. There is nothing in sub-section (4) imposing any limitation upon the time when, or the conditions under which, the notice there mentioned is to be served. What possible object an Income-tax Officer can serve by sending a notice to an assessee to produce his accounts and documents before such assessee has made any return at all, it is difficult to follow. Why should the legislature have intended, without using express and clear language, to prevent the Income-tax Officer from calling upon an assessee to produce accounts and documents under this sub-section after he has made his return? The object of his doing so is made clear by the next section. If the Income-tax Officer is satisfied that a return is correct, he is directed to make the assessment under sub-section (1).

How is he to be satisfied, if he has any suspicion or grounds for dissatisfaction unless, when he sees the return and has some materials before him for forming a judgment, he can ask to see the books of the assessee? *A fortiori* unless he is to obtain private information from secret and possibly unreliable sources, how is he to form a belief under section 23, sub-section (2), that the return made under section 22 is incorrect, or incomplete, unless at least he can inform himself by the obvious and elementary method of calling for the books. It is to be observed that the notice which he may serve on the person who made the return under section 23 (2), is only to be served when the officer has reason to believe that the return made is incorrect or incomplete, and unless the return is, on the face of it, ridiculous or the Income-tax Officer has secret information, it is impossible for him to form any honest belief on the subject at all, unless he can secure some materials. It seems to us, therefore, that a great part of the duties of the Income-tax Officer would be rendered practically unworkable if it were to be held that sub-section (4) of section 22 could only be worked before a return had been made. The Government Advocate made a valuable criticism upon the argument. The machinery is slightly different where there is a company and where there is an individual assessee. In the case of a company, under sub-section (1), the principal officer is required to prepare and furnish every year on or before the 15th day of June in each year a return, whereas the return under sub-section (2) required of an individual is only to be made in response to a notice served upon him by the Income-tax Officer to make such return within a specified period. It follows, therefore, that if the argument put forward were to be accepted, the words "before the 15th June in each year" would have to be inserted in the case of the principal officer of any company in sub-section (4) of section 22, and that, although there is not a word in the statute to suggest it, if the Income-tax Officer did not call upon every company in his jurisdiction before the 15th June to produce accounts and documents required by him—a most burdensome requisition—he would, after such company had made its return, be prevented for the rest of that fiscal year from doing so.

On this matter we have no hesitation in quoting from the excellent Commentary of Mr. Vishvanatha Sastri, a Vakil of Madras, the author of *The Law and Practice of Income-tax*, published in 1922, dealing with this very question of the evidence in support of a return under section 22. He expresses this opinion:

"The Income-tax Officer is empowered to call upon the assessee (whether or not he has made a return) to produce such documents and accounts as he may require within the period specified in the notice requiring their production. Sub-section (4) prevents the Income-tax Officer from calling upon an assessee to produce books of account going back for a period of more than three years prior to the accounting period. There is, however, no such limitation upon the power to call for documents. In the case of trades and business, the Income-tax Officers require in addition to the profit and loss account a copy of the balance-sheet. Provided the return which has been made is a correct one, the submission of these documents cannot prove detrimental to the taxpayer."

We agree with that opinion. The matter seems to us to be simple, and really it would seem almost unarguable, if it were not for the decision arrived at by the Patna High Court in *Brijraj Ranglal v. Commissioner of Income-tax*,

Bihar and Orissa. (1) We respectfully differ from that decision and find it somewhat difficult to follow. The fallacy, if we may say so, is based upon the assumption which, in our view, there is nothing to justify that a notice under section 22 (4) can only be given to a person who has not made a return, and that if it is given after a return has been filed, such a notice is illegal. One of the reasons given in the judgment is that the words "having made a return," which occur in the third case of default in section 23* (4), create some antithesis between such default and the preceding default of failing to comply with a notice under section 22 (4). We cannot follow this. It is not a case where any antithesis is required. To our minds the words merely mean what they say, and have no other object than that, which the Government Advocate pointed out, of emphasising the fact that the third default, namely, failure to comply with sub-section (2) of section 23, can only be made by a person who has already made a return, because it is only such a person who can be served with a notice in accordance with sub-section (2) of section 23. It is wrong to say that they are meaningless. Many reasons might be given why the draftsman thought it right to insert them where they are. One reason is this that an Income-tax Officer may have honest reason to believe that the return which he has received, has been made by the assessee and is incorrect or incomplete, when the return was not in fact made by the assessee at all, and although the Income-tax Officer might have honest reason to believe that it was, and might legitimately serve on such person a notice under sub-section (2) of section 23, such person would have a complete answer to an assessment against him to the best of the Income-tax Officer's judgment under sub-section (4) by proving that he had not made the return. No doubt this illustration is an extravagant one in the sense that it is unlikely to occur, but in a country in which false documents are so common and false charges are so frequently made out of enmity, it may well have been considered quite possible that a discharged servant or some other enemy, might deliberately send in a false return purporting to be by an assessee, which would appear to be incomplete or incorrect on the face of it, for the purpose of inducing the Income-tax Officer to give him, what is called in this country, "*Dik*". At any rate, if such a case should occur, the language which we have just cited is appropriate thereto. We, therefore, answer the first part of the question in the affirmative and the second in the negative, agreeing with the Commissioner. The assessee must pay the costs. We fix the fee at Rs. 150. Ten days will be allowed for filing of the certificate.

[228] IN THE HIGH COURT OF JUDICATURE AT CALCUTTA.

Before Sir George Rankin, Kt., Chief Justice, Mr. Justice C. C. Ghose and Mr. Justice Mukherji.

[9th January, 1928.]

The Commercial Properties, Ltd.

.. Assessee*

v.

The Commissioner of Income-tax, Bengal

.. Referring Officer.

Income-tax Act (XI of 1922), Secs. 9 and 10—Registered company owning properties, letting and collecting rents—Income, if derived from business—Assessability as income derived from property.

* (1928) I.L.R. 55 Cal. 1057; 32 C.W.N. 413; A.I.R. (1928) Cal. 456.
1. 2 I.T.C. 458.

A registered company whose sole object was to acquire lands, build houses and let them to tenants, owned three properties, the sole business of the company being the management and collection of rents from the said properties. On an assessment to income-tax under section 9 of the Act, the company claimed that they were carrying on a business assessable under section 10 and not under section 9.

Held, that the Company was to be assessed under section 9, its income being derived from its ownership of building.

In re, Kaladan Suratee Bazaar Co., Ltd., 1 I.T.C. 50, Referred to.

Case stated under section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bengal, for the opinion of the High Court.

CASE.

At the request of "Commercial Properties, Limited", I have the honour to refer to the Hon'ble High Court, under section 66 (2) of the Indian Income-tax Act (XI of 1922) a question of law, hereinafter stated, arising out of the assessment of the above company to income-tax for the year 1926-27.

2. The facts of the case are as follows:—"Commercial Properties, Limited" hereinafter referred to as "the Assessee" is a registered Company of which the sole object is to acquire land, build houses and let premises to tenants in Calcutta or elsewhere in India. The sole assets of the Assessee consist of three properties, and the sole business of the Assessee is the management and collection of rents from the said properties. The Assessee contended before the Income-tax Officer that they were carrying on a business and should be assessed under section 10 of the Income-tax Act. The Income-tax Officer disallowed their contention and assessed them under section 9. The Assessee preferred an appeal to the Assistant Commissioner who upheld the order of the Income-tax Officer, finding that the Assessee were not a "business" within the meaning of the Income-tax Act. The Assessee then applied to me to state a case to the Hon'ble High Court, which is now being stated.

3. The question of law which is referred to the Hon'ble High Court is as follows:—

On the above facts should the Assessee be assessed under section 9 or under section 10 of the Indian Income-tax Act, 1922, in respect of the property owned by them?

4. I am required by the Act to state my opinion in the matter which is as follows:—

Even if the assessee is held to be a business, they must be assessed in respect of the property owned by them according to the special provisions relating to property.

T. Ameer Ali, for the assessee.

Sir B. L. Mitter (Advocate-General) with H. R. Pankridge (Standing Counsel) and S. M. Bose, for the Crown.

JUDGMENT.

RANKIN, C. J.—This is a case stated by the Commissioner of Income-tax, Bengal, and the question for decision is whether or not the assessee is liable to income-tax under section 9 of the Indian Income-tax Act, 1922 or only under section 10 of that Act.

It is the function of the Commissioner to find the facts and it is for this Court to accept his findings on all matters of mere fact.

The facts stated are that the assessee, The Commercial Properties, Limited, is a registered Company of which the sole object is to acquire land, build houses and let premises to tenants in Calcutta or elsewhere in India. The sole assets of the assessee consist of three properties and the sole business of the assessee is the management, and collection of rents from the said properties.

The opinion of the Commissioner of Income-tax is that "even if the assessee is held to be a business they must be assessed in respect of the property owned by them according to the special provisions relating to property".

It will be observed that section 6 of the Indian Income-tax Act states that "the following heads of income, profits and gains shall be chargeable to income-tax in the manner hereinafter appearing, namely." Then comes six heads of which the third is "Property" and the fourth is "Business". By section 9 "the tax shall be payable by an assessee under the head 'Property' in respect of the *bona fide* annual value of property consisting of any building or lands appurtenant of which he is the owner, other than such portions of such property as he may occupy for the purposes of his business"; and it goes on to lay down the method in which the *quantum* of the tax is to be computed. It points out, for example, that where the property is in the occupation of the owner, or where it is let to a tenant and the owner has undertaken to bear the cost of repairs, then one-sixth is to be the deduction for repairs. In like manner, a deduction is to be allowed for insurances. Questions of mortgage interest and ground rent are covered and there are specific provisions as regards allowance to be made for parts of the property being unoccupied from time to time. Again, it is to be noted that the "annual value" is to be deemed to be the sum for which the property might reasonably be expected to let from year to year so that this class of property is not to be taxed on the basis of *de facto* rent alone, and it is further provided that where the property is in the occupation of the owner for the purposes of his own residence, the annual value is not to be deemed to be more than ten per cent. of the total income of the owner. I mention these matters to show that special computations which arise in the case of house property are dealt with under section 9 which is a particular, detailed and special scheme for ensuring that any property which comes within that section shall be taxed in a particular way.

Section 10 which deals with Business—"profits or gains of any business carried on by him"—is also provided with certain rules as to allowances to be made before computing profits. These rules, in so far as they refer to house property, refer to "the premises in which such business is carried on" but with regard to insurance premiums, land revenue, rates and taxes refer to buildings and premises "used for the purposes of the business".

In the present case we have a company which owns three estates. It does not appear that any part of that property is outside the definition given in section 9. It is found to let the houses from time to time, to see to the payment of rents and doubtless the doing of repairs. If that is carrying on a business, then this Company carried on a business in the sense in which every landlord or owner of this type of property must necessarily carry on business. We know from section 9 itself that it is applicable to property which is let out to tenants

and it has been argued before us that when one looks at the case-law one finds that, at all events, where the owner is a company and the objects of the company include the object of owning and managing house property, then the income that is derived from the tenants is an income that is derived from business. It is in that way that it is contended that these assesseees should be charged under section 10. It is said that if the question were to arise under section 10 these assesseees would not be liable to pay income-tax at all so that no income-tax would be recovered in respect of any of these estates, the reason being, that, in point of fact, they have traded so unsuccessfully during the year in question that they have actually made a loss. This is certainly a very important question from the point of view of the Treasury because if this argument be right then it will depend to some extent upon the success of the management whether or not the public treasury should derive any income-tax in respect of house property of this character. It is obvious, too, that if we were to depart in such a case as this from the careful provisions contained in section 9 for purposes of computing the correct figure in the case of house property on which tax is to be levied we will get under section 10 all sorts of complicated questions special to house property upon which the law will be absolutely at large. In my judgment the words of section 6 and section 9 and section 10 must be read so as to give some effect to the contrast that is there made between income, profits and gains from "Property" and from "Business"; and I entirely refuse my assent to the proposition that because it happens that the owner of a property is a company which has been incorporated for the purpose of owning such property, therefore the income derived from "property" must be regarded as income derived from "business". In my judgment, income derived from "property" is a more specific category applicable to the present case.

The cases to which we have been referred are cases in England with, I think, one exception which is a case from Burma. The case in Burma, *In re Kaladan Suratee Bazaar Co., Ltd.*,⁽¹⁾ arose out of the Excess Profits Duty Act, 1919. The Excess Profits Duty Act laid a special tax upon the profits of business, and although it contained a special protection for the earnings of a man in his profession there was no special provision applicable to the case of an owner of property. There was a Company called the Kaladan Suratee Bazaar Co., Ltd., which owned certain plots of land and stalls at Moulmein at a bazaar there. Its income was derived from the rents of houses and bazaar stalls belonging to it and the Financial Commissioner not disputing that it was subject to income-tax under section 9 maintained that it was liable to excess profits duty because it was a "business" within the meaning of the Excess Profits Duty Act. The decision of the Court was that these two Acts were to be interpreted in the same way. It was pointed out that a person or a Company drawing income from house property was clearly not contemplated in the Indian Income-tax Act as carrying on a business but was treated as a person who derived income from the property and, in the same way, when the question of Excess Profits Duty had to be decided the Court determined that the Company was not carrying on a business within the meaning of that Act. It was pointed out that if the mere letting of stalls was carrying on a business within the meaning of the Act, then every person who had invested his capital in house property was liable to excess profits duty when his income rose above the mini-

(1) 1 I.T.C. 50.

mum limit. It was further said that a man who had invested his capital in house property and who kept a rent office and a staff of rent collectors, clerks, etc., for the purpose of letting out his houses and collecting the rents was not carrying on a business. He was merely taking the ordinary steps necessary for enjoying the income from his property. That, therefore, is the Indian case which bears upon this question and it is not in favour of the assessee.

Of the English cases to which we have been referred, the first is the case of *Commissioners of Inland Revenue v. Sangster*.⁽²⁾ That was a decision of Mr. Justice Rowlatt. It was the case of a man who was an inventor and who derived considerable sums of money from royalties paid to him by Companies of which he was a Manager. He had sold one invention, it is true, but that was a good long time ago; and in these circumstances it was contended that he carried on the business of an inventor and was therefore liable under the provisions of the Finance Act of 1915 to excess profits duty. That argument was rejected, Mr. Justice Rowlatt saying that he was not carrying on a business because he was an owner of royalties and that he was not carrying on a business because he was a share-holder in a certain Company.

Much reliance has been placed, however, upon certain cases of which the case of *Commissioners of Inland Revenue v. Korean Syndicate Limited*⁽³⁾ is the chief. There, again, was a question not whether the Company was liable to pay under Schedule A of the Income-tax Act or under Schedule D but whether it was liable to excess profits duty as carrying on a trade or business at all. It was a very complicated case and I do not propose to set out the facts, but it is clear that the Company was originally incorporated to get and work a concession in Korea but ultimately it obtained a share and had an agreement with a co-sharer to do the actual working of the concession; a certain sum was to be paid to it under this agreement. The document purported to be a lease and the sum by the document was called a royalty; but, on a close examination of the particulars by the Master of the Rolls Lord Sterndale, it was held that the Company was carrying on in this particular way the business of obtaining a working concession for which it had been incorporated, that the document was not really a "lease", that the payments were not truly and strictly "royalties" and that, therefore, it was not entitled to say that it was outside the scope of the excess profits duty. Very similar are the decisions under the Corporation Profits Tax imposed by section 52 of the Finance Act of 1920. There tax was put *prima facie* upon every British Company which carried on trade or business or anything of that kind. Cases arose on the border line, such as a case where a Company having put up money to build an Indian Railway and an Indian Railway having been built by the Secretary of State and managed more or less successfully, the Company was now in the position of receiving under its agreement certain payments, and it was contended on the one hand that it was not carrying on a business at all. It has ultimately been decided by the House of Lords that if you look at the matter from the beginning as a whole the Company was carrying on the business of financing this Indian Railway and that although it had finished finding the finance and only had to receive what was due to it under the agreement it could not be said that it was no longer carrying on business.

(2) 12 Tax Cas. 208; (1920) 1 K.B. 587. (3) 12 Tax Cas. 181; (1921) 3 K.B. 258.

In my judgment, these cases are not authorities to the effect that as between the word "Property" and the word "Business" in section 6 of the Indian Income-tax Act, 1922, a case of this character is to be put under the word "Business". It comes more directly and specifically under the word "Property". In my judgment, the mere fact that the house owner is a Company does not change the incidence of the tax in the way contended for. The income of the assessee is income derived from its ownership of buildings and their curtilages. To obtain such income a certain amount of management is always necessary but the Act does not regard such income as profits of management. To own houses one must buy or build them but the Act does not regard such income as profits of investment.

In my opinion, the Income-tax Commissioner was right and we should answer the question which he has put to us that the assesseees are to be assessed under section 9 of the Act.

The assesseees must pay the costs of the Reference.

GHOSE, J.—I agree.

MUKERJI, J.—I agree.

Morgan & Co., Attorneys for the assesseees.

G. C. Gooding, Attorney for the Crown.

[229] IN THE COURT OF THE JUDICIAL COMMISSIONER,
NAGPUR.

Before Mr. Hallifax, Additional Judicial Commissioner and Mr. Mohiuddin, Additional Judicial Commissioner.

[25th January, 1928.]

Seth Nanhelal and Ghasiram of Hoshangabad

*Assesseees**

v.

The Commissioner of Income-tax, Central Provinces and
Berar

Referring Officer.

Income-tax Act (XI of 1922), Sec. 13—Money-lender keeping accounts on mercantile basis—Interest debited to each debtor and credited in Interest Khata—Sums shown as due but not received in cash or by adjustment, if assessable.

The assesseees carrying on money-lending business were keeping their accounts on the mercantile basis, debiting interest to each debtor's account and carrying these entries subsequently to the Biyaj Khata or interest account. In their return of income for the years 1923-24, 1924-25 and 1925-26 the total shown in the interest account was shown as their yearly income and assessments were made accordingly. In the assessment for 1926-27 the assesseees sorted out the cash receipts from the Biyaj Khata, and claimed that they were assessable only on the total of those cash items alone. The Income-tax Officer rejected this claim and made an assessment on the total of all the entries in the Biyaj Khata.

Held, that the sums shown in the accounts as having fallen due but not received or paid in cash or by adjustment of accounts could not be treated as income assessable under the provisions of section 13 of the Act.

* (1928) 24 N.L.R. 176; A.I.R. (1928) Nag. 241.

Subramanyam Chettiar v. Commissioner of Income-tax, 2 I.T.C. 365, Considered and explained.

Case [Miscellaneous Judicial Case No. 27 of 1927] stated under section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Central Provinces and Berar, for the opinion of the High Court.

CASE

Seth Nanhelal and Ghasiram of Hoshangabad have grain and money-lending business which they transact from Hoshangabad and seven other places in that district. They keep very regular and closed accounts on what is known as the mercantile system, i.e., they debit interest to the debtor's account.

- (i) when it is paid in cash,
- (ii) when it is acknowledged by him and account is signed by him even though payment in cash is not made (*Hisab* and *Ruzu Bahis* are kept for this),
- (iii) when it is added to the principal at the time of renewing or taking a fresh bond,
- (iv) when at the end of the year (Diwali in respect of cash and Baisakh in respect of grain) account is carried forward, and
- (v) when it is added to the principal at the time of filing suit in civil court.

N.B.—Interest of (ii) and (iii) kinds is called "*Makbula*" (acknowledged) and interest of (iv) and (v) kinds is called "*Gcr-Makbula*" (unacknowledged).

The whole interest is then taken to *Biyaj Khata*, i.e., interest account, and the yearly income is thus ascertained. For the purposes of income-tax assessments, the Seths have been returning this income and have been assessed in the past:—

For 1923-24 on Rs.	96,010
„ 1924-25 „	83,491
„ 1925-26 „	80,382

2. For assessment during 1926-27 the Seths did not return the income from interest as shown in their *Biyaj Khata* which is still maintained as before. They merely sorted out the cash receipts from this *Biyaj Khata* on pieces of paper and omitted other items and returned the total income at Rs. 14,093-9-8. The Income-tax Officer did not accept this return. He took the income from interest as shown in the *Biyaj Khata* and assessed the Seths on an income of Rs. 93,333 (under his order dated the 8th of October 1926).

3. Against this assessment, an appeal was preferred on two grounds, i.e.,

- (i) The Income-tax Officer should have assessed the amount of interest actually realized and received by the petitioners in cash from the debtor.
- (ii) The Income-tax Officer in any case should not have taken the amount of interest merely acknowledged in *Hisab Bahi* or *Ruzu Bahi* for the purpose of saving limitation and which did not amount to fresh contracts.

4. The Assistant Commissioner did not allow these objections though he reduced the taxed income by Rs. 1,000 remitted against one Beharilal Bazaz (*vide* copy of his order dated the 20th of January 1927).

5. On the 28th of February 1927 an application under section 66 (2) of the Income-tax Act was made in which I am asked to refer the following three points to the High Court, viz.:

“(i) Whether interest which has not been actually received or realized by the assesseees but which has been merely entered in their account books for the purpose of proper account-keeping can be said to be income, profit or gain which is liable to assessment of income-tax.

(2) Whether interest which has not been actually received or realized by the assesseees but which is merely acknowledged by the debtors to save limitation can be said to be income, profit or gain which is liable to assessment of income-tax.

(3) Whether interest which has not been actually received or realised by the assesseees but which has been taken into consideration in executing or renewing a bond by the debtors in order to save limitation can be said to be income, profit or gain, which is liable to assessment of income-tax.”

6. In order to ascertain the exact system of accountancy an enquiry was held. Meanwhile on the 7th of April 1927 another application was made and I was asked to refer a fourth point to the High Court, viz.:

“Whether interest which has not been actually received or realised by the assesseees but which is included in decretal amount can be said to be income, profit or gain, which is liable to assessment of income-tax.”

7. As regards this point it may be said at the outset, that inasmuch as the application to refer it to the High Court, was not made within 30 days of the passing of the order under section 31 of the Income-tax Act, as required by section 66 (2) of the Act, the applicants are not justified in making this request; and this point will, therefore, be omitted from this reference. The three points raised in the application, dated the 28th of February 1927, are referred for the decision of the Hon'ble the Judges of the High Court.

8. In arguing the case before me the learned counsel for the applicants seemed to rely very much upon the decisions in the cases of (1) *Secretary to the Board of Revenue, Income-tax, Madras v. Al. Ar. Rm. Arunachalam Chettiar & Brothers*(1), and (2) *Pandit Pandurang v. Commissioner of Income-tax, Central Provinces*(2). In regard to the first of these decisions I would point out that it relates to the Act of 1918. That Act contained no section corresponding to section 13 of the Act of 1922. In the absence of such a provision the High Court of Madras held that to constitute “income” there must be a receipt, actual or constructive. This decision would have caused extreme embarrassment not so much to the Income-tax authorities as to that large class of assesseees whose accounts are maintained according to the mercantile system of accountancy. That system, as is well known, is not concerned at all with actual or constructive receipts and payments, but with sums that have fallen due to or by the party concerned. The ruling of the Madras High Court as it stood meant that assessment on the basis of the mercantile system of accountancy was illegal. In order to return their income, therefore, all assesseees maintaining accounts on the mercantile basis, that is, all Companies, all European businesses, and a large number of Indian businesses also, would have had to write a fresh

set of accounts for income-tax purposes separate from those maintained for their own purposes, and based moreover on an unscientific and inconvenient system, according to which casual circumstances may inflate the income in any year enormously. To get over this difficulty section 13 was inserted in the Act of 1922, under which a man keeping accounts on the cash system is assessed on the cash basis and a man keeping his accounts on the mercantile system, on the basis of book debits and credits. This ruling is therefore obsolete and irrelevant. The other decision (apart from the fact that it related to interest that had not actually fallen due, and not like the present case to interest that has fallen due) determined no question relating to the manner of computing income, but merely that such a question is a question of law. Consequently it also throws no light on the present case. For similar reasons the case of *Pydah Venkatachalapathi Garu v. Commissioner of Income-tax, Madras*(1) which relates to the Act of 1918 and to the cash system of accountancy, is also irrelevant. In the present case, as stated above, it is at the end of the year, or the accounting period or after an acknowledgment or renewal of bond, that the interest which has already fallen due is taken into account and is entered against the debtor and is also afterwards brought into the interest accounts. Thus in each subsequent year, the principal plus the interest becomes the capital and the whole amount carried interest, and this goes on for years. The result is that after some time the original amount of advance is lost sight of and interest, except of last year, is hardly ascertainable except with reference to books of accounts of several years which it is not possible always to obtain. The questions as formulated are vague and to some extent really overlap.

9. I beg now to give my opinion as required by the Act on each of the questions:

Point (1). Since the assesseees keep their accounts practically on the mercantile system, sums that have fallen due to them, and have consequently been debited against their debtors, are rightly treated as income, and the question whether such sums have been received actually or constructively is entirely irrelevant. (The same principle, of course, applies equally to sums due by the assesseees). Under the cash system of accountancy it was no doubt held by the Madras High Court in the case of *Commissioner of Income-tax v. Pydah Venkatachalapathy Garu* (1) mentioned above that where compound interest is payable by a debtor to his creditor with yearly rests, and the creditor makes entries in his books of accounts adding to the principal amount the interest which has accrued due at the end of the year, but does not receive payment either in cash or by counter-credit in the debtor's accounts, a mere entry of such interest in his books of accounts does not make such interest taxable income within the purview of the Income-tax Act. In this particular case the creditor has been making counter-credits in the debtor's accounts also. These are as good as adjustments, and adjustments are "constructive receipts", *Secretary, Board of Revenue, Madras v. Al. Ar. Km. Arunachalam Chettiar and Brothers*,(2) and therefore the sums in question would be income, and as such taxable, even under the cash system of accountancy.

Point (2). This question is expressed in a misleading manner. It has not been proved that the acknowledgements of the interest due by the debtors

(1) 1 I.T.C. 185.

(2) 1 I.T.C. 75.

are taken merely to save limitation. Apart from this attempt to twist matter's this question really raises the same point of principle as No. 1 and the answer is the same as the answer to No. (1).

Point (3). This again is in principle the same question, and as before the answer is that since the accounts are maintained on the mercantile system these sums are taxable under section 13, and that they would, as a matter of fact, be taxable as constructive receipts even if the assessee maintained his accounts on the cash system.

Sir B. K. Bose and J. Sen, for the Assesseees.

Rai Bahadur D. N. Chowdhary, for the Crown.

JUDGMENT.

The Commissioner of Income-tax referred three questions to this Court under section 66 of the Income-tax Act on the application of the assesseees. They were stated as follows by the assesseees, and sent on by the Commissioner without alteration:

1. Whether interest which has not been actually received or realized by the assesseees but which has been merely entered in their account books for the purpose of proper account-keeping can be said to be income, profit or gain, which is liable to assessment of income-tax.

2. Whether interest which has not been actually received or realised by the assesseees but which is merely acknowledged by the debtors to save limitation can be said to be income, profit or gain which is liable to assessment of income-tax.

3. Whether interest which has not been actually received or realised by the assesseees but which has been taken into consideration in executing or renewing a bond by the debtors in order to save limitation can be said to be income, profit or gain, which is liable to assessment of income-tax.

(2) The assesseees later put in an application for the reference of a fourth question which the Commissioner rejected because it had not been made within the time allowed. That question was stated as follows:

Whether interest which has not been actually received or realised by the assesseees but which is included in decretal amount can be said to be income, profit or gain, which is liable to assessment of income-tax.

(3) In his statement of the case the Commissioner points out that the three questions he submitted for decision are all the same. That is true, and the fourth is also exactly the same, but they can not be said even to contain a question of principle. What they come to is this. If interest has fallen due to an assessee, the fact being established in one of four different ways, and he has entered the amount of it in his account books as due to himself, but has not realised it and may never realise it, can the amount of that interest be called the income, profit or gain of the assessee? The answer is fairly obviously in the negative.

(4) But it is quite clear from the Commissioner's statement of the case and the arguments advanced on his behalf that the question he and the assesseees intended to put was this. If interest has fallen due to an assessee but has not been paid to him and he shows the amount due in his Interest Ledger (*Byaz Khata*) on the credit (*jama*) side for himself, according to the mercantile system of accounts which he has adopted, is the amount so shown

to be treated as income, profit or gain under section 13 of the Income-tax Act? The Commissioner would answer this question in the affirmative.

(5) That answer is based on a misreading of section 13 of the Act; and perhaps a greater misunderstanding of the judgment of the High Court of Madras in *The Commissioner of Income-tax, Madras v. Subramaniam Chettiyar*(1). That judgment was cited in this Court as supporting the proposition that section 13 of the Act means what it says, which hardly needs support. In that case certain sums of interest which had not been paid in cash were shown in the assessee's books as received, by book-transfer or otherwise, in accordance with the method of accounting regularly followed in those books; the learned Judges naturally held that any sum shown as income or profits in the books must, under section 13 of the Act, be regarded as income or profits whether it had been received in cash, or what is called "constructively received".

(6) But in the present case the sums of interest are not shown as income or profits received in any way, whether in cash or by adjustment of accounts; they are shown as still due, that is to say, not yet received and perhaps never to be received. The most that can be said of them is that they are shown in the accounts as assets, and that not of the amounts stated, but of so much of them as may be recovered hereafter.

(7) Section 13 merely lays down that sums shown in the accounts as received, whether actually or constructively, (and there is little real difference) must be treated as income. It would be to stultify the legislature to suggest that it lays down that sums shown as not received at all must be treated as income. Our answer to the particular question in this case is that the sums shown in the accounts as having fallen due but not received cannot be treated as income. The costs of these proceedings must be paid by the Commissioner of Income-tax. The pleader's fee will be two hundred rupees.

[230] IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Sir Murray Coutts Trotter, Kt., Chief Justice, Mr. Justice Wallace, Mr. Justice Beasley, Mr. Justice Jackson and Mr. Justice Srinivasa Ayyangar.

[1st February, 1928.]

T. K. E. Ibrahimsa Ravuttar

.. Assessee*

The Commissioner of Income-tax, Madras

.. Referring Officer.

Income-tax Act (XI of 1922), Secs. 2 (1) and 4 (3) (viii)—Assessee carrying on money-lending business—Loans on usufructuary mortgages with simultaneous lease back to mortgagor—Assessment as income derived from business of money-lending—Claim of exemption as rent from agricultural land—Income, if agricultural income.

The assessee whose chief source of income was money-lending business lent money on usufructuary mortgages of agricultural land with no stipulation for interest, the income from the mortgaged properties to be taken and enjoyed by him. The Income-tax Officer purporting to look into the substance of these

(1) 2 I.T.C. 365.

* (1928) 51 Mad. 455; 54 M.L.J. 524; A.I.R. (1928) Mad. 543.

transactions held that the income derived therefrom was really part of the profits and gains of the money-lending business carried on by the assessee and not agricultural income exempt from assessment.

Held, [Jackson, J., dissentiente] that the income sought to be assessed was rent derived from land used for agricultural purposes and hence exempt from assessment under Sec. 4 (3) (viii) of the Income-tax Act.

Subramanya Sastrigal v. Commissioner of Income-tax, Madras, 2 I.T.C. 152 Overruled.

Case [Referred Case No. 11 of 1927] stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

CASE.

In accordance with the order quoted above, I have the honour to refer the following case for the opinion of the Hon'ble the Judges of the High Court.

2. The petitioner is T. K. E. Ibrahimsa Ravuttar of Trichinopoly. His chief source of income is business in money-lending. He returned an income of Rs. 1,804 from this source.

3 He maintains no accounts for this business and the exact amount of his income therefrom cannot be determined. It has been estimated at Rs. 40,000. This was an enhanced estimate made under section 31 on appeal by the Assistant Commissioner. Copies of the original order of assessment passed by the Income-tax Officer, Trichinopoly and of the Assistant Commissioner's order on the appeal are appended—Exhibits A and B.*

4. The petitioner makes a practice of lending money on the security of documents which purport to convey to him, in lieu of interest, the right to the possession and enjoyment of agricultural land. Simultaneously, or nearly so, another document is executed in each case, purporting to be a lease of the land by the mortgagee to the mortgagor, subject to the payment, in the guise of rent, of sums equivalent to interest at a fixed rate on the money lent. The Income-tax Officer and Assistant Commissioner looked to the substance of these transactions and found that the income derived from them was really part of the profits and gains of the business carried on by the assessee and not income derived from land used for agricultural purposes. The form of usufructuary mortgage and lease back while no doubt partly intended to protect the capital was found to have been adopted as a cloak to conceal the real source and character of the income in question. The amount of the income from such of these mortgages as were disclosed was found to be Rs. 6,285.

5. The petitioner appealed to me under section 32 against the enhancement and at the same time required me, under section 66 (2), to refer certain questions for the opinion of the High Court. The appeal and the application for reference were dismissed. Copies of my orders are appended—Exhibits C and D.*

6. In the application under section 66 (2) the first question propounded ran as follows:—

"When a mortgage of lands is with possession carrying higher stamp duty than a simple mortgage, can the Income-tax Officer go behind the registered instrument and institute an enquiry to see whether it is really a simple mortgage and

assess the mortgagee for income-tax, calculating interest upon it as if it was a simple mortgage?"

The petitioner's case then was that the Income-tax authorities were debarred by the form of the transactions from any enquiry into their substance. He disputed the right of the Income-tax Officer to "go behind the transaction" and look to its substance and its real character. He did not dispute the correctness of the finding that the sum in dispute was income from business. It was on this footing that the case was put before me by Dewan Bahadur O. Tanikachalam Chettiar, the petitioner's Advocate.

7. The High Court on the application of the petitioner has now called upon me to refer the following question:—

"If an assessee takes a usufructuary mortgage from a mortgagor and leases it back again to that person receiving rent from him, is that rent assessable to income-tax?"

8. I propose to assume that the mortgage contemplated in the question is a mortgage of land used for agricultural purposes and either assessed to land revenue in British India, or subject to a local rate assessed and collected by officers of Government as such, in the language of section 2 (1) (a) of the Act. If the property mortgaged were a house, for instance, it is presumably beyond dispute that the rent received would be assessable either under section 12 as "income from other sources," or under section 9 as representing the whole or part of the annual rental value of the property.

9. The question thus formulated was not raised before me in the application under section 66 (2), and I submit that the petitioner is not entitled to raise it now. I submit further that section 45 of the Specific Relief Act, quoted in the order of the Court, cannot be invoked in this case, since the remedy provided by section 66 of the Income-tax Act was available to the petitioner.

10. I have refrained from troubling the Court with an application in this matter under rule 8 of the Rules of procedure prescribed for these references because the Court has ruled on a previous occasion that a preliminary objection of this character can be entertained at the hearing of the reference itself.

11. In view of the facts and circumstances found in paragraph 4 above, I am of opinion that the exemption of agricultural income under section 4 (3) (viii) of the Indian Income-tax Act which is designed to protect the income derived from agricultural land subject to payment of land revenue from double taxation cannot apply to income which in fact and in truth is part of the profits and gains of the money-lending business carried on by the assessee. I am of opinion that the decision of this Court in the case of *Subramanya Sastrigal v. Commissioner of Income-tax, Madras*(1) is applicable to this case, and that the question should be answered in the affirmative.

K. S. Krishnaswami Aiyangar for *A. Krishnaswami Aiyar* with *T. M. Venugopala Mudaliar* and *M. Balasubramanya Mudaliar*, for the Assessee.

M. Patanjali Sastri, for the Crown.

The JUDGMENT of the CHIEF JUSTICE, WALLACE, J., BEASLEY, J., and SRINIVASA AYYANGAR, J., was delivered by

SRINIVASA AYYANGAR, J.—The question referred in this case for the opinion of the High Court is as follows:—“If an assessee takes a usufructuary mortgage from a mortgagor and leases it back again to that person receiving rent from him, is that rent assessable to income-tax?” When the case came on at first before three of us, on hearing arguments to some extent, it became clear that the decision and opinion of the three judges of this Court in *Subramanya Sastrigal v. Commissioner of Income-tax, Madras*(1) required reconsideration and it was thereupon this case was directed to be posted for being heard before a bench of five judges. It is correct, as pointed out by the Income-tax Commissioner in his letter of reference, that the question proceeds on the assumption that the subject-matter of the mortgage is land used for agricultural purposes and either assessed to land revenue in British India, or subject to a local rate assessed and collected by officers of Government as such in the language of section 2 (1) (a) of the Income-tax Act. We are now satisfied that the answer to the reference in the case above referred to was given without full discussion or consideration. Section 6 of the Income-tax Act XI of 1922 is the charging section. Though in that section interest on securities, property, business and other sources of income are all indicated as heads of income chargeable with income-tax, still the section begins with the words “Save as otherwise provided by this Act.” In clause (3) of section 4 it is however provided that the Act shall not apply to certain classes of income and the sub-clause (viii) thereof is ‘agricultural income.’ It follows from this that the classes of the income specified in section 6 are liable to the tax only subject to the exceptions set out in section 4, clause (3); in other words, even though some income is capable of falling within one or more of the classes assessable to income-tax under section 6, still if such income should also be agricultural income the same will be exempt from assessment. The expression ‘agricultural income’ is defined by section 3, clause (1) as including any rent or revenue derived from land which is used for agricultural purposes. Section 2 which is the definition section in the Act, as usual in all enactments, sets out the definitions with the qualification “unless there is something repugnant in the subject or context.” It was argued by Mr. Patanjali Sastri for the Commissioner that as in section 10 read with section 6 the Act provides that the tax shall be payable by an assessee under the heading of ‘Business,’ in respect of the profits or gains of such business, the exemption under sub-clause (viii), cl. (3) of section 4 of agricultural income, must, having regard to the context, be construed as referring only to such agricultural income as is not capable of being properly designated as income from business. There is no warrant for such a contention. The expression ‘agricultural income’ in section 4 has no special context apart from all the classes of income exempted from assessment, and the expression ‘agricultural income’ the definition of which is in question does not occur in any context in either section 6 or in section 10. It is a well-established canon of interpretation that any question of context or repugnancy in the subject can arise only if the same expression that is defined occurs or is repeated in any particular section. The only question then is whether, having regard to the facts of this case, the rent accruing to the mortgagee from agricultural land is or is not liable to exemption as agricultural income. It has been assumed for the purposes of the reference that the

lands are used for agricultural purposes and the income under reference is the amount agreed to be paid as rent by the mortgagor-lessee in respect of such lands. Having regard to the amount reserved as rent under the lease deed there can be no question that it is rent derived from land which is used for agricultural purposes. There can be no question also in this case of the motives of the assessee in bringing about a particular arrangement, because as has been pointed out by the House of Lords in more than one case it is not proper to take such motives or objects into consideration, and a subject is entitled, if he can in any legal manner, to circumvent the incidents of a particular taxing or financing Act. According to section 6 income from business is assessable only if it be not agricultural income, and to invert this and contend, as was argued in this case, that agricultural income will not be exempt from assessment if it be business income would lead to a complete deadlock. We must take it that the usufructuary mortgage referred to in the question is a simple usufructuary mortgage and that there is no stipulation as to any interest and that the income accruing from the properties mortgaged is to be taken and enjoyed by the mortgagee with possession. No doubt as indicated in the question itself the land subject to the mortgage is leased back again by the mortgagee to the mortgagor and therefore, even reading both the instrument of mortgage and the instrument of lease together as indicated by the Judicial Committee in *Abdulla Khan v. Basharat Hussain* (1) it must appear that the amount sought to be assessed is legally only rent. If it be rent—and in this case there is nothing to show that it is anything else—then on the considerations set out already it follows that it is not assessable. Our answer therefore to the question referred is in the negative.

The assessee will have his costs, which we fix at Rs. 300.

JACKSON, J.—The question for decision is, shortly, whether a money-lender who enters into the familiar form of transaction, a mortgage and lease back, is exempt from paying income-tax upon its proceeds. I could understand the assessee's claim if the transaction were strictly divided into two parts. First, as usufructuary mortgagee he enters into possession of the property and looks to its agricultural yield for his interest; then he prefers to realise that yield by putting a tenant into possession and enjoying the rent. But this division into two parts was not held to be the correct method of interpretation by the Judicial Committee in *Abdulla Khan v. Basharat Hussain* (1) when it ruled that the mortgage and lease were parts of one and the same transaction. Viewed as a whole the transaction is one by which the money-lender obtains interest on the money advanced; there was never any real transfer of possession, and the so-called rent has nothing to do with agricultural purposes, being entirely based upon the money-lending firm's rate of interest. In my opinion it is not agricultural income but profits of business and therefore not exempt. A Full Bench of this Court held the same view in *Subramanya Sastrigal v. Commissioner of Income-tax, Madras* (2) and I am not persuaded that that decision is wrong.

(1) I.L.R. 35 All. 48.

(2) 2 I.T.C. 152.

[231] IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Sir Murray Coutts Trotter, Kt., Chief Justice, Mr. Justice Beasley and Mr. Justice Madhavan Nair.

[2nd February, 1928.]

Rm. Ar. Ar. Rm. Ar. Arunachalam Chettiar

... Assessee*

v.

The Commissioner of Income-tax, Madras

... Referring Officer.

Income-tax Act (XI of 1922), Sec. 4 (3) (i)—Sums entered in accounts in the name of a charity—If property held under trust—Irrevocable dedication in trust, if a question of law.

The assessee, a Nattukottai Chetty banker, on an assessment to income-tax contended that certain sums of money shown in his accounts in the name of a charity—Tiruvadanai-Tiruvalur Tiruppani account—were trust funds dedicated and held by him as trustee. The Income-tax Officer found on the facts of the case that there was no absolute and irrevocable dedication enforceable in a court of law.

Held, that the question whether there was an irrevocable trust or not was a question of fact.

Case [Referred Case No. 5 of 1927] stated under Sec. 66 (1) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, for the opinion of the High Court

CASE.

In pursuance of the order quoted above I have the honour to refer the following case for the opinion of the High Court under section 66 (1) of the Indian Income-tax Act, 1922.

2. The petitioner is a banker and is carrying on business in Rangoon and Colombo among other places. For the purposes of his Rangoon business the petitioner draws large sums of money from the assets of his Colombo branch, which consist partly of his own capital and partly of borrowed capital. On the amounts so drawn by the Rangoon branch interest is debited as having been paid to Colombo in the Rangoon accounts. In connection with his assessment to income-tax for 1923-24 the petitioner claimed a deduction of Rs. 71,340 from the income of his Rangoon branch as interest so paid to the Colombo branch. The Income-tax Officer, Sivaganga, disallowed this claim on the ground that adjustments of interest between the branches of an assessee's business should be ignored in computing his taxable income. On appeal before the Assistant Commissioner the petitioner alleged that the money sent from Colombo to Rangoon was money borrowed by him at Colombo. This he could not prove. The Assistant Commissioner therefore found that the money sent was the petitioner's own money and upheld the Income-tax Officer's decision.

The petitioner thereupon applied to the Commissioner for a review of the assessment under section 33 of the Income-tax Act and also asked for a reference to the High Court under section 66 (2). My predecessor held that it would be fair to assume that part of the money, in the proportion that the borrowed capital at Colombo bore to the total capital employed at that place,

was borrowed capital, and to allow the claim to that extent. He accordingly asked the Assistant Commissioner to examine the petitioner's accounts and report the exact amounts of his own and borrowed capital employed at Colombo. The accounts showed that the petitioner's own capital at Colombo was Rs. 10,72,797 and his borrowed capital Rs. 10,61,849. It was then noticed that the borrowed capital included a sum of Rs. 2,51,609 shown in the accounts in the name of "Padigampetta Sivalaya Fund" and it was elicited that this fund represented petitioner's own money entered separately in his accounts with a view to expenditure on certain temples. As there was no legally constituted trust dedicating the money for those purposes, the Commissioner proposed to treat this sum as petitioner's own money, but on the petitioner executing a document creating a trust he refrained from doing so. The nature of the other items included in the petitioner's list of borrowed capital was not then investigated.

3. For the assessment of the year 1925-26 based on the accounts of 1924-25 the petitioner made a return of his income and produced his Colombo accounts as evidence in support of it. The accounts showed that during the year of account the petitioner had permanently transferred to his Rangoon branch a part of his assets in the Colombo branch; in other words, that moneys had been remitted from Colombo to British India. The petitioner had to his credit in the Colombo branch unassessed profits of previous years. These profits are taxable under section 4 (2) of the Income-tax Act, if they are received in British India within three years from the end of the year in which they accrued or arose. The Income-tax Officer proposed to tax a part of the remittance as such profits. The petitioner stated that the remittances to Rangoon were out of his borrowed moneys at Colombo and that the transfer of such borrowed sums from Colombo to Rangoon was effected in order to get rid of the constant disputes regarding the interest on borrowed capital which arose in assessing the income of the Rangoon branch. To test the correctness of this explanation the Income-tax Officer had to investigate the extent of the borrowed capital employed by the petitioner in his Colombo business. His investigation disclosed that the petitioner had certain sums credited in his Colombo accounts in the names of two funds, *viz.*, "Tiruvadanai-Tiruvalur Tiruppani account" and "Oorkadai Chel account" besides the Fund referred to above. The petitioner was treating these sums as borrowed capital and had included them as such in the lists furnished by him in connection with his assessment for 1923-24.

The petitioner explained that the amount to the credit of the "Tiruvadanai-Tiruvalur Tiruppani account" was money dedicated by him for a charitable purpose, *viz.*, the renovation of the temples at those places, that he was holding the sum as trustee, and that in that capacity he had invested the money in his business for interest; in other words, that he as an individual carrying on business had borrowed the money from the trust for which he was the trustee. In support of his statements the petitioner produced an agreement entered into in November 1905 between himself and his paternal uncle A. R. A. R. S. M. Somasundaram Chettiar. According to this agreement the parties decided to find Rs. 500 each monthly for a period of 10 years for each of the two charities, Thiruvadanai and Tiruvarur Temple Tiruppanis, *i.e.*, at the end of the period of 10 years each of them undertook to contribute

Rs. 1,20,000 or Rs. 60,000 for each of the two charities. The petitioner did not however set apart a sum of Rs. 500 every month for each of the two charities. In fact nothing was heard of this agreement till the year 1917. In March 1917 the petitioner opened a separate ledger in his Colombo accounts and entered in it a sum of Rs. 60,000 under the head "Tiruvadanai-Tiruvalur Tiruppani account". It will be noted that under the agreement he was to have found a sum of Rs. 1,20,000 for the renovation of the two temples. There was nothing to show whether and if so how he contributed the balance of Rs. 60,000. Nor was there any evidence as to what the other party Somasundaram Chettiar had done to fulfil his part of the agreement. The sum entered as stated above in the petitioner's Colombo accounts together with the interest thereon amounted to Rs. 1,17,820 on 28—5—1924. On this date the whole amount was transferred to the petitioner's Rangoon branch and interest is shown in the Rangoon accounts as having been paid on this amount. No separate accounts were maintained for the so-called Trust Fund. The Tiruvadanai Temple Tiruppani (renovation) had been completed but the work was done with the aid of other funds. The Income-tax Officer found that the agreement above referred to had not been given effect to by the parties themselves, that there had been no dedication of any money for the renovation of the temples and that an irrevocable trust had not been created. He therefore treated the amount shown under this head as petitioner's own capital.

As regards the "Oorkadai Chel account" the petitioner stated that the details of the amounts for which a lump credit was given in his Colombo accounts under that head were to be found in his Headquarter accounts, that a part of the moneys in that account was borrowed from other persons and that the balance represented amounts set apart by him for various charities. He was not however able to give particulars of the sums so set apart and in explanation said that his father and his uncle Somasundaram Chettiar separated about 25 years ago from the then common family "Ar. Ar.", that some of the amounts in question might have been set apart by the common family and some by himself. The petitioner did not adduce any evidence that the sums that he alleged were set apart for charitable purposes, were moneys over which he had no dominion and which he could not resume at his pleasure. The Income-tax Officer held that there were no valid trusts created and in the absence of full particulars he determined that half the total amount standing to the credit of this account should be treated as borrowed capital and the other half as petitioner's own.

As the sums standing in the names of these funds were remitted from Colombo to Rangoon the Income-tax Officer treated the whole of the interest credited to the first fund and half of the interest credited to the second fund, during the year of account and the previous three years, as profits received in British India and taxed them under section 4 (2) of the Income-tax Act. He also disallowed the interest shown in the Rangoon accounts as having been paid on these funds, subsequent to the date of remittance.

4. The petitioner appealed to the Assistant Commissioner against this order and contended that the sums remitted to British India from the two funds in question were trust moneys and interest derived therefrom should not be included in his income and assessed to tax. The Assistant Commissioner admitted this contention and revised the Income-tax Officer's order under the impression that the question whether the funds constituted valid trusts was

concluded by my predecessor's order revising the assessment of 1923-24. This impression was not correct because, as stated above, the nature of these funds was not then enquired into. This will be evident from the order of my predecessor dated 24—12—1924 in which he remarked "the sum of Rs. 10,61,850 was borrowed from outsiders and from a *fund* set apart by the assessee for charity." It was then assumed that there was only one such fund and that the moneys in the names of the other two funds were borrowed from outsiders.

5. My predecessor who perused the records of the case proposed to revise the Assistant Commissioner's order under section 33 of the Income-tax Act and accordingly issued a notice to the petitioner calling on him to show cause why the interest debited in the Rangoon account as having been paid to the "Tiruvadanaï-Tiruvalur Tiruppani" and "Oorkadai Chel" accounts amounting to Rs. 8,880 and Rs. 16,104 respectively, which was allowed by the Assistant Commissioner on appeal, should not be included in the petitioner's taxable income and why the sum of Rs. 1,17,820 remitted to British India from the first account and Rs. 1,74,756 being half the sum remitted from the second account should not be treated as foreign profits and assessed to tax. The petitioner appeared in response to this notice through his Vakil and again set up the plea that the funds in question were trust funds. My predecessor held that the petitioner had not proved the existence of irrevocable trusts and by his order dated 8th April 1926 enhanced the taxable income of the petitioner by Rs. 24,984, the sum which had been allowed by the Assistant Commissioner as interest paid to the two funds by the Rangoon business. He however refrained from taxing the remittances from out of these accounts as he accepted the petitioner's plea that the transfer was made in the genuine belief that the sums would be treated as borrowed capital and with a view to avoid disputes about the computation of his Rangoon profits similar to those that arose in previous years.

6. The petitioner then moved my predecessor to refer to the High Court under section 66 (1) of the Income-tax Act three questions which he alleged arose out of his order under section 33. My predecessor declined to do so for the reasons contained in his order dated 16th May, 1926. Thereupon the petitioner moved the High Court under section 45 of the Specific Relief Act to direct the Commissioner to state a case to the High Court under section 66 of the Income-tax Act. The High Court has ordered me to refer the following questions:—

(1) Whether by reason of the decision of the Commissioner dated 24th December 1924 he is not estopped or precluded from re-opening the question of the liability to assessment of the funds referred to in paragraphs 3 and 4 of the Commissioner's order dated the 8th April 1926.

(2) Whether a fund set apart for the purposes of a particular trust and so entered in the accounts and treated as trust fund for several years cannot be held to be property held under trust or other legal obligation for religious or charitable purposes, income from which is exempt from assessment under section 4 (3) (i) of the Income-tax Act.

(3) Whether there is a distinction in law between a fund set apart for charity and a fund kept as a 'reserve' for charity.

7. *Question (1).* It will be clear from the facts stated above that the nature of the two funds in question was never before the subject of any

enquiry, and my predecessor's order dated 24th December 1924 did not preclude him from investigating the nature of the two funds on fresh facts being placed before him. The doctrine of estoppel or *res judicata* applies only when a question in dispute between two parties had previously been the subject-matter of a decision in a court of law. The Commissioner of Income-tax acting under section 33 is not a court. He is only an executive officer entrusted with certain functions under the Act and in the exercise of those functions he has to take into consideration various factors to which a court need not attach much weight. In particular he has to see that the work of the department is finished within the year and assessees are allowed to get on with their business. If, owing to the absence of sufficient materials in a particular year, he decides a question in favour of the assessee in order to avoid delay, I do not think he is estopped from examining the same point in detail in the following year when he has more time and materials before him. I would therefore answer this question in the negative.

8. *Question (2)*. The assumption underlying this question, *viz.*, that the funds referred to above were set apart for the purposes of particular trusts and treated as trust funds was never admitted by my predecessor. His finding on the facts of the case and the evidence before him was that certain sums belonging to the petitioner were shown by him in his accounts in the names of certain charities and that the petitioner had not proved to his satisfaction that he had created specific trusts. Further, it is not correct to say that the sums were treated as trust funds. As already observed the nature of these funds was not examined before. The petitioner is of course spending money on certain charitable objects but that by itself does not prove that the funds from which these expenses are met are trust moneys which he was bound by law to apply in the manner he did. There was no other proof that valid trusts had been created. In the case of the "Tiruvadanai-Tiruvalur Tiruppani account" the petitioner did not spend any money out of the account on the objects with which, it is alleged, the fund was set apart. As already observed the renovation of the Tiruvadanai temple has been practically completed without the aid of this money. There was no proof that the petitioner contributed anything towards the renovation of the temple at Tiruvalur. The agreement of 1905 relied on by the petitioner was not given effect to and the conduct of the parties shows that it was never their intention to enforce its terms. The petitioner may have recently decided to fulfil his part of the agreement to a certain extent by the execution of a trust deed but this does not alter the position as it was when my predecessor decided the question. I accept the findings of the Income-tax Officer and my predecessor that the petitioner had not proved the existence of the alleged trusts. The income derived from the funds in question is not therefore exempt under section 4 (3) (i) of the Income-tax Act.

9. *Question (3)*. I am of opinion that this question is based on a misconception of my predecessor's order dated 8th April 1926. What he intended to convey was that the petitioner proposed to spend the sums entered against the "Tiruvadanai-Tiruvalur Tiruppani account" and the "Oorkadai chel account" on certain charitable objects at the time and to the extent he chose and that there was no absolute and irrevocable dedication of those sums for the charities which any other person interested in those charities could enforce in a court of law. The fact that a person shows in his accounts a part of

his money as intended to be spent on charitable purposes does not necessarily mean that he has placed upon himself a legal obligation to spend that money for those purposes. His action might amount only to a pious wish and there is nothing to prevent him from using it on any object he likes. On the other hand if he makes an open and irrevocable declaration that he has set apart money for a certain specified charity, he may be said to have created a trust and undertaken a legal obligation which the beneficiaries would be in a position to enforce. My predecessor was of opinion that the amounts in question were not so set apart or absolutely dedicated for charities but were merely kept in reserve to be used on certain charitable objects. In my opinion there is a distinction in law between sums dedicated for charities and those merely entered in a person's accounts in the names of certain charities.

K. S. Krishnaswami Ayyangar and V. Rajagopala Aiyar, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

BEASLEY, J.—Although there are three questions referred to us the only question upon which we are called upon to give a decision is the second question, namely, whether a fund set apart for the purpose of a particular trust and so entered in the accounts and treated as a trust fund for several years cannot be held to be property held under trust or other legal obligation for a religious or charitable purpose, income from which is exempt from assessment under section 4 (3) (i) of the Indian Income-tax Act. This question in our view is entirely answered by the findings which appear in the order of the Income-tax Commissioner. He has dealt with this trust as a trust which was revocable. Dealing with one fund, namely, the fund which was set aside for the purpose of repairing the temple, he points out—and it is beyond question—that when it was necessary to repair that temple, money was drawn from another fund for the purpose of so doing and not from this fund. He also points out that if there was a dedication at all no one knew of its existence except the person who dedicated it, namely, the assessee. It seems to us that it was quite open to the assessee at any time he chose to entirely alter the character of that money. The trustees of the temple did not know of its existence. We are far from saying that it is necessary in order to create a trust that the person in whose favour the trust is created should know about it. But at the same time it is a circumstance to be taken into consideration by the Income-tax Commissioner in coming to a conclusion as to whether or not there had been a real dedication and as to whether or not the fund so created or the trust so said to be created can be revoked. This is purely a question of fact and we are bound to say that in our opinion the Income-tax Commissioner has rightly decided that question. The answer accordingly to this question would be that this fund is not exempt from assessment under 4 (3) (i) of the Indian Income-tax Act. The assessee will pay to the Commissioner Rs. 250 costs.

[232] IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Sir Murray Coutts Trotter, Kt., Chief Justice, Mr. Justice Beasley and Mr. Justice Madhavan Nair.

[2nd February, 1928.]

Rao Saheb A. S. Alaganan Chetty

*Assessee**

v.

The Commissioner of Income-tax, Madras

Referring Officer.

Income-tax Act (XI of 1922), Sec. 10 (2) (ix)—Assessee doing business as carrying contractor—Payment to rival contractor for not competing with him—If deductible as business expenditure—Capital expenditure.

The assessee doing business as a carrying contractor paid Rs. 12,000 to a rival contractor to induce the latter not to compete with him. As a result of the non-competition of this rival, he obtained the carrying contract at a rate higher than the previous year's rate enabling him to make larger profits. On an assessment to income-tax, the aforesaid sum was claimed as a deduction in the computation of his taxable profits under Sec. 10 (2) (ix) of the Act.

Held, that the payment of this sum not being for the purpose of working the contract but for obtaining it, was capital expenditure and not a permissible allowance under Sec. 10 (2) (ix).

City of London Contract Corporation, Ltd. v. Styles, 2 Tax Cas. 239; John Smith & Son v. Moore, 12 Tax Cas. 266; 'Countess of Warwick' Steamship v. Ogg, 8 Tax Cas. 652, Referred to and applied.

Case [Referred Case No. 12 of 1927] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

CASE.

Under Sec. 66 (2) of the Income-tax Act (XI of 1922) I have the honour to state the following facts and to request that the opinion of the Hon'ble the Judges of the High Court may be obtained on the questions appended thereto.

2. The petitioner, Rao Saheb A. S. Alaganan Chetty has been doing business continuously since December 1, 1907 as carting contractor to the Kanan Devan Hills Produce Company, Limited. His relations with the company during this period were defined in a series of contracts, some of which were for one year and some for longer periods. In and before the year beginning 1st December, 1920, there was apparently no competition for the contract. The contract for the year fixes the rate of payment to the contractor at "Rs. 15 per ton gross for produce and goods of whatever kind or description transported from Kodaikanal Road Railway station to Bottom station and *vice versa*." For the year following (1921-22) the rate is shown in the contract as Rs. 14-8-0 per ton gross. For the year 1922-23 the rate is Rs. 14-12-0. This fall in the rate to a figure below Rs. 15 per ton is said to be due to the fact that a competitor, whom I call X, had offered to do the work at the lower rates, and although not successful in obtaining the contract for himself, had nevertheless forced the petitioner to reduce his demand. The next contract was for a period of three years beginning from the 1st December, 1923. The rate specified therein is "Rupees Fifteen (Rs. 15) per ton gross for transport of all goods of whatever kind or

**(1928) 55 M.L.J. 66; 27 L.W. 776; A.I.R. (1928) Mad. 902.*

description and bulk from Kodaikanal Road Railway station to Bottom station, and Rupees Fourteen and annas twelve (Rs. 14-12-0) per ton gross for transport of all produce and goods of whatever kind and description and bulk from Bottom station to Kodaikanal Road Railway station." These rates are evidently more favourable to the contractor than those of the two previous years and little below those for the year 1920-21.

3. It is asserted, and I do not propose to dispute, that before this contract was given to the petitioner an arrangement was arrived at between him and X under which he agreed to pay a sum of Rs. 12,000 to X on condition that the latter would abstain from competing for the contract.

4. In the year of assessment, 1926-27, the petitioner's accounts were examined with a view to determining the income of the previous year. It was found that the sum of Rs. 12,000 referred to in the previous paragraph had been adjusted on October 1, 1925, to the credit of X. It is admitted that this entry does not represent a payment of cash but for the purposes of this case it is agreed that payment of the whole sum shall be taken to have been made on the date mentioned.

5. In the assessment made upon X in the assessment year 1926-27 this sum of Rs. 12,000 was brought into computation as a sum received by X in the year of account 1925-26.

6. The petitioner claimed that this sum of Rs. 12,000 should be deducted in computing his income as being expenditure allowable under sub-clause (ix) of clause (2) of section 10 of the Act. The Income-tax Officer disallowed this claim on the ground that the expenditure "relates to the preliminary process of acquiring the contract and is not expenditure incurred in the year of account during the regular course of business." The Income-tax Officer's decision was upheld on appeal by the Assistant Commissioner.

7. The petitioner now contends that the decision of the Assistant Commissioner is erroneous in point of law. His Vakil has agreed to the submission of the following two questions as being those arising out of the order under section 31:—

(i) Whether the sum of Rs. 12,000 paid in the year of account in the circumstances stated above was expenditure (not being capital expenditure) incurred solely for the purpose of earning the profits and gains of the petitioner's business, so as to be allowable as a deduction under section 10 (2) (ix).

(ii) Whether the petitioner should be declared not liable to tax on the above amount on the ground that the same amount was treated as income of the payee and was taxed in his hands.

8. My opinion on the above two questions is as follows:—

(i) The question is briefly whether the expenditure referred to is capital expenditure. The Vakil contends that it was not, because the money was spent and the petitioner has nothing by way of capital to show for it. In other words he did not, by means of this payment, acquire an asset. This contention appears to me to overlook the distinction between "capital" and "capital expenditure." The case of the *'Countess of Warwick' Steamship Co., Ltd. v. Ogg*(1) and the judgment of Lord McLaren in the case of the *Granite Supply Association v. Kitton* (2) may be cited as authority for the view that capital expenditure

(1) 8 Tax Cas. 652.

(2) 5 Tax Cas. 171.

does not necessarily mean expenditure resulting in an increase of capital. It is further asserted that X, the payee, had no power to dispose of the contract, and therefore the payment cannot be said to have been made with the object of securing the contract. It was, however, admittedly made to eliminate competition and thus to enable the petitioner to obtain the contract. I am therefore unable to see that this argument has any force. It is no doubt true that as a result of this payment the petitioner found himself in a position to derive increased profits, but the payment was certainly not part of the actual business operations by means of which these profits were derived. I consider that the payment was of a capital nature and that the question should be answered in the negative.

(ii) The fact that a particular sum was taxed as a "revenue" receipt in the hands of X has no bearing on the question whether the same sum should be treated as "revenue" expenditure in assessing the petitioner. The answer to that question must depend, I consider, on whether the expenditure claimed is covered by statutory provision. My view therefore is that the deduction cannot be allowed on the ground on which it is here claimed. I may support this view by citing a remark of Mr. Justice Rowlatt's in the case of *Thomas v. Richard Evans & Co., Ltd.*(1) "The money that comes in may be . . . capital expenditure of the person who pays it and income of the person who receives it."

Vere Mocket and L. S. Veeraraghava Aiyar, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

THE CHIEF JUSTICE.—The facts in this case are simple and raise a point in a very clean form. The assesseees were persons who used to try for and frequently obtain contracts from a large tea-growing company for the cartage of their tea down to Kodaikanal Road Station for entrainment. The contracts were made at a flat rate which varied from year to year, so much per ton. In the year we are concerned with there was, and apparently there had been in former years also, a rival contractor who is referred to as X who is regarded obviously as likely to be a very dangerous competitor for the contract and in order to induce him not to compete the assesseees paid him down a sum of Rs. 12,000. That they say they are entitled to recover as being expenditure not in the nature of capital expenditure incurred solely for the purpose of earning such profits or gains. The result was that as Mr. X did not compete, they had the whole field to themselves; they got the whole contract and were able by screwing up the figures in former years to make more profits than they would have done in those former years. As a matter of fact the probability is that the extra profits they got just about squared with the Rs. 12,000 they paid to Mr. X. The principles that apply are contained in the statute of course and are much illuminated in our opinion by two cases, one in the Court of Appeal and another in the House of Lords in England to which we shall refer and which seem to us to explain in the clearest possible way the distinction between capital payments and expenditure not being capital, where it is conceded that in every case the expenditure is incurred solely for the purpose of earning the profits. I have really read the material part of the Indian Statute. It is section 10 (2) (ix): "(2) Such profits or gains shall be com-

(1) 5 A.T.C. 314.

puted after making the following allowances" and the only one we are concerned with is sub-section (ix), "any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains." The first English case to which I propose to refer is a case of the *City of London Contract Corporation, Limited v. Styles* (1) in the Court of Appeal in 1887 before a very powerful Court consisting of Lord Esher, Bowen, L.J. and Fry, L.J. The first passage I am going to read is an observation made by Bowen, L.J. in the course of the argument and it appears to me to be as clear and sharp-cut a distinction as any to be found in the other cases. In that case the assessee took over a business of another company which had a number of unexecuted contracts on hand and the taking-over company paid a lump sum of money to the out-going company to obtain the benefit of those contracts and claimed it as a deduction. Lord Justice Bowen in the course of the argument said this:—"You do not use it (that is, the money which had bought the contractual rights) 'for the purpose of' your concern, (which means 'for the purpose of carrying on your concern') but you use it to acquire the concern." Similarly Lord Esher at page 244: "Here is a clear statement that the difference between money expended in the year in order to earn income which was to be received in the year, and the income so received was £1,28,000. That is the net profit within the year, that is the sum upon which income-tax is to be paid; and it is as plain as plain can be that you cannot deduct from those net profits so arrived at any part of the capital which you so invested, whether you paid it or not for the purchase of the business which you were obliged to purchase before you could begin the difference between expenditure and income year by year. If you do not darken it with words, it is as plain as plain can be."

Now I pass to a case in the House of Lords, *John Smith & Son v. Moore*. (2) The facts I need not really go into because the passage I am going to cite from Lord Sumner is really what directly bears on this case. "They (the company) said, much as has been said in this case, that before profits can be made out of working a contract, the contract has to be got and the payment of its price is the root of the profits. The court held that this sum was paid with the rest of the aggregate price to acquire the business and thereafter profits were made in the business; the sum was not paid as an outlay in a business already acquired, in order to carry it on and to earn a profit out of this expense as an expense of carrying it on. The same is true of the appellants. The whole price paid, in cash or in account, was a sum employed or intended to be employed as capital in the trade of the company, and therefore cannot be deducted in ascertaining profits for income-tax or excess profits duty."

I only wish to refer just in passing to one other case which is the case of the ship-builder and the buying of all the contracts, *'Countess of Warwick' Steamship Company v. Ogg*. (3) It is the judgment of a single Judge but it is a judgment of Rowlatt, J., a very great authority in income-tax cases in which he has specialised for so many years. I will not quote his language but the short point was this. The Steamship Company in question had arranged for the purchase of a steamship on the very common system whereby the ship-builders are paid a lump sum in part payment as soon as the keel is laid in the yard and the rest of the price is paid in instalments as the fabric is gradually

(1) 2 Tax Cas. 239.

(2) 12 Tax Cas. 266; (1921) 2 A.C. 13.

(3) 8 Tax Cas. 652.

built up. After about £30,000 had been paid to the ship-builders which was a very small portion of all that would ultimately have to be paid there was a slump in freights and the owners came to the conclusion that it would be impossible for them to carry on the business of running this ship as a freight-earning ship at any profit whatever and they therefore sought to get out of the liability for paying for a thing that in their hands would be perfectly useless. The £30,000 of course was gone but in order to get out of the contract they had to pay another £30,000 and the argument that found favour was that this was not a loss which could be brought into the profit and loss account, because although it is difficult to say, it resulted in any increase of capital or plant in the nature of capital to the ship-owners, it was incurred in relation to that part of their business.

That being the state of affairs, what is the position here? Applying the one which, to my mind, is the easiest to apply, Bowen, L. J.'s test, surely any plain man would say that this money was paid not for the purpose of working the contract but of getting it at all; it was the price that had to be paid to obtain the contract. This appears to us to answer the first question propounded to us and to answer it adversely to the assessee. In that view it is unnecessary to answer the second question. We therefore answer the first question in the negative confirming the decision of the Income-tax Commissioner and order the assessee to pay Rs. 250 by way of costs to the Income-tax Commissioner.

BEASLEY, J.—I agree.

MADHAVAN NAIR, J.—I agree.

[233] IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Justice Sir Cecil Walsh, Kt., K.C. and Mr. Justice Iqbal Ahmad.

[3rd February, 1928.]

Baghat Halwai

Assessee.

Income-tax Act (XI of 1922), Sec. 23—Assessee producing evidence in support of return—Evidence rejected by the Income-tax Officer and assessment on estimate from personal inspection—Determination of assessable income, if a question of law—Proceedings under Ch. IV if judicial proceedings.

Where the Income-tax Officer rejecting the evidence of the assessee and his witnesses in support of his return formed an opinion from his own inspection of the assessee's place of business and on the basis thereof determined the assessable income

Held, that the determination of a fair figure as the assessable income was one of fact.

Proceedings under Ch. IV of the Act (Assessment proceedings) are judicial proceedings in the colloquial sense only and are not judicial proceedings in the strictly scientific sense of the term, so as to raise questions in appeal to some higher tribunal as to whether the authority making the assessment has decided against the weight of evidence, or decided a fact of which there is no evidence or has disregarded evidence which ought to have been taken into account.

In this case stated by the Commissioner of Income-tax under section 66 (2) of the Act, the High Court refused to entertain the reference and declined to issue notice to the assessee on the ground that no question of law arose.

Case [Miscellaneous Case No. 81 of 1928] stated under section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, United Provinces, for the opinion of the High Court.

CASE.

Baghat Halwai who keeps a sweetmeat shop returned his income as Rs. 700 in the year ending March 31, 1927. When called on to prove his return, he made a sworn statement and produced three witnesses to give oral evidence in support of his return but did not produce any accounts as he does not maintain any. The witnesses were three Brahmins, one a Pujari, the others writers of accounts in two shops.

2. The statements of the assessee and his witnesses are contained in Appendix A.* The assessee swore that his sales amounted to Rs. 20 to Rs. 25 per diem. The witnesses made estimates, one fixing Rs. 15 with Rs. 20, 25 or 30 on the occasions of festivals, another Rs. 20, 25 or 30 with larger sums on special occasions, while the third stated that he had been at the assessee's shop on a few occasions and had heard him say on three days that his sales amounted to Rs. 22, 21 and 25. The Income-tax Officer who along with the Assistant Income-tax Officer had visited the shop and on the basis of his own observation there had estimated daily sales of Rs. 50 to Rs. 60, rejected this evidence because "it is evident from the statement of the witnesses that they have little or no idea of the assessee's business, or if they do they have attempted to minimise the sales," and estimated the profits to have been Rs. 2,400, an assessment being made accordingly.

3. The assessee appealed to the Assistant Commissioner of Income-tax who rejected his appeal in the following terms:—

"In response to.....the notice.....under section 23 (2) he (the assessee) produced three witnesses in support of his return of income. Their evidence was not accepted by the Income-tax Officer and the reasons given by him are clear enough from his assessment note. Two of the witnesses deposed in a manner which is in the highest degree incredible. No one goes about shouting what his daily income is. If the appellant did it must have been a preparation for the present case. When they heard him is not clear from their statement. The third witness deposed to what he had seen in the appellant's shop. This need not necessarily mean the gross sales. The oral evidence is, therefore, inconclusive. Question then arises whether in the circumstances the Income-tax Officer was debarred from estimating the appellant's income. There is no provision in the Act to debar him from doing so. On the other hand the responsibility is laid on him for estimating the profits of an assessee's business in the best manner possible. In the written arguments which have been furnished by the accountant and auditor whom the appellant has engaged to represent his case it is stated that in a fiscal statute the benefit of doubt is the right of a subject. In support of this statement is cited the case of *Partington v. Attorney-General* (1). It is clear from it that what the Judges were considering in that case was the construction of statutes. So far as construction of statutes goes the liability of the appellant is clear. No question of benefit of doubt arises. For instance, there is nothing in the Act to show that the income from the selling of sweetmeats is exempt. It cannot be said that that ruling descends to such details as the making of estimates. An estimate is at

*Not printed.

(1) (1869) 4 E. & I. App. H.L. 100.

the outside merely an approximation to what is believed to be one's income and no question of benefit of doubt arises in making it. It was open to the appellant to produce definite evidence and when he failed to do so it was equally open to the Income-tax Officer to estimate his income. In estimating the income he has had regard to the locality in which the business is carried on and apparently to the appearance of the shop. These are factors of considerable importance in making an estimate."

4. The petitioner has now asked for a reference to the High Court on the following points of law:—

(a) That the proceedings under Chapter IV consisting of sections 18 to 39 are the 'Judicial proceeding' and in face of oral evidence when there is none on the records to contradict the same, the Income-tax authorities are not empowered to disbelieve that evidence.

(b) That merely not keeping the accounts the persons cannot be disbelieved in face of their solemn declaration unless otherwise there is on record any proof to contradict the declaration of an assessee.

(c) That the benefit of doubt is the right of the subject and if the subject cannot be brought within the letter of law, he cannot be taxed and the assessee is not come to the letter of law and therefore cannot be taxed.

5. The assessee has accepted the foregoing statement of the case. He was further asked whether he accepted the points of law as stated in the following paragraph but he would prefer that the points of law should be as follows:—

"1. Whether in view of the fact that the proceedings held under Chapter IV of the Income-tax Act of 1922 are "Judicial Proceedings", the Income-tax authorities are justified in relying on his casual inspection and in rejecting the whole mass of consistent statements on oath of witnesses produced by the assessee without describing the nature of his own inspection and without allowing an opportunity to the assessee to test the correctness of the conclusions arrived at by him.

"2. Whether the Income-tax Officer is justified in making an estimate of the assessee's profits on the basis of his own "observations" without drawing up and putting on the record an inspection note soon after the inspection, and without giving a chance to the assessee either to test its correctness or to explain it.

"In case your honour does not agree with the view that the proceedings held under Chapter IV of the Income-tax Act are "Judicial Proceeding", your honour may be pleased to split up ground (1) with the following two grounds—

(1) Whether the proceeding held under Chapter IV of the Indian Income-tax Act XI of 1922 are "Judicial Proceedings",

(2) Whether the Income-tax authorities are justified in relying on his casual inspections and in rejecting the whole mass of consistent statements on oath of witnesses produced by the assessee describing the nature of his own inspection and without allowing an opportunity to the assessee to test the correctness of the conclusions arrived at by him."

The points of law as stated by the petitioner appear to be argumentative and contain phrases open to objection. Moreover the points are fully covered by the questions of law which, in the opinion of the Commissioner, arise and which are stated by him.

6. These questions of law are:—

(1) Was the Income-tax Officer, who relied on the evidence afforded by his own inspection, justified in rejecting the evidence produced by the assessee in support of his return, and

(2) Was the Income-tax Officer justified in making an estimate of the assessee's profits on the basis of his own observations?

7. In the opinion of the Commissioner the evidence produced by the assessee is vague and of no value and the answer to the first question should be in the affirmative. The evidence obtained by personal observations is the most reliable evidence in the case of assesseees who follow this trade and the Income-tax Officer would have failed to perform his functions properly if he had not used that evidence. The answer to the second question, therefore, should also be in the affirmative.

JUDGMENT.

While recognising the consideration of the Commissioner of Income-tax for the assessee, and his arguments, and his desire to be fair to the members of the public, and without intending any reflection upon his discretion in submitting this case, we decline to issue notice, on the ground that no question of law arises.

The controversy has arisen with regard to the profits of a sweet-seller, who keeps no books, and who in accordance with an admittedly correct notice issued to him did the right thing and brought up his witnesses, one of whom was a Pujari, and two were writers of accounts in two shops. They gave their view of the man's daily income. At the most, that can only be a matter of opinion. The Income-tax Officer did not believe them. He went and looked at the shop himself, or employed somebody to look at the shop, and tried to form an opinion as to the sort of business that was being carried on. He disagreed with the assessee and his witnesses. In other words, he did not believe their oral statements and formed an opinion from his own inspection, which, after all, is evidence. He thereupon determined the sum payable by the assessee, on the basis of an assessment of the total income of the assessee, taking into consideration the admission of the assessee and his witnesses, which the Income-tax Officer did not think went far enough, and the results of his own personal observation. The assessee is discontented with the result. Many taxpayers suffer from the same complaint. It is a pity, but it is often the case that they regard anybody in authority, and particularly the Income-tax Officer as their natural enemy. As a matter of fact, it is sound tactics, when a man is the final tribunal of a question of fact on which you have to pay income-tax, to humour him as much as possible, not to treat him as an enemy, but to try and please him as you would a friend; but in pursuance of this discontent, he has argued and submitted to the Commissioner the view that the proceedings in Chapter IV of the Income-tax Act are judicial proceedings. This is not a question of law, and the Income-tax Commissioner has rightly refused to state the question in that shape. They are judicial proceedings in the colloquial sense, because the Income-tax authorities have to make up their minds judicially, with fairness to the public and to the assessee, between whom they stand, after taking all the facts, or such facts as they can, into account, but they are not judicial proceedings in the strictly scientific sense of the term, so as to raise questions in appeal to some higher tribunal as to whether the gentleman making the assessment has decided against the weight of evidence, or decided a

fact of which there is no evidence, or has disregarded evidence which he ought to have taken into account. To open the door for one moment to such a contention would turn this Court into a court of appeal of fact with regard to every assessment in which the assessee was dissatisfied with the decision.

Section 23 (1) and section 23 (2) deal with the two cases in which, on the one hand, the Income-tax Officer is satisfied with the return and in which, on the other hand, he is not satisfied with the return, and in each case, after following the procedure laid down, he, and he alone, is to determine the amount of the assessment and the sum payable. It is a question of fact of which he is the sole judge, and he must use his best judgment first to obtain, and secondly to weigh, the available evidence. It is to some extent a private inquisition, it is confidential, it is not supposed to be disclosed to the public, and it is certainly not open to review, especially because frequently, the Income-tax Officer is compelled to draw inferences and to consider evidence which might not be justified by the Evidence Act. For the very reason that it is a sort of private inquisition, Income-tax authorities are expected to be scrupulously fair to members of the public who treat them fairly, but there is a duty corresponding to the right, and if an assessee wants to be treated fairly the least he can do is to treat the Income-tax Officer fairly and lay the facts fully before him. There is no suggestion here of any departure from the procedure laid down by the Act, and the questions of law propounded by the Commissioner are really not questions of law at all. Anybody who has to decide a question of this kind, after a *quasi* judicial weighing of the evidence, is entitled to reject the evidence produced by the assessee. As was once said in a case by a well-known Judge in England, there is no rule of law compelling a Judge to accept evidence, even though it is uncontradicted, which he believes to be a pack of lies. Similarly, provided the Income-tax Officer makes fair observation of his own in an honest attempt to arrive at a decision, he is perfectly justified in doing so and in acting upon it. The sooner it is understood that these are questions of fact, and questions of fact only and that the slightest attempt to open the door to appeals to this Court on what are alleged to be mixed questions of law and fact, but are really only questions of a fair figure of assessment, must be discouraged, the better; otherwise we should be inundated, or the Commissioner would be inundated, with applications to state cases. We are clearly of opinion that no question of law arises, and therefore we ought not to issue notice. Let the case be returned to the Commissioner.

[234] IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Mr. Justice Harrison and Mr. Justice Dalip Singh.

[6th February, 1928.]

Duni Chand

... Assessee.*

v.

The Commissioner of Income-tax, Punjab and North-West Frontier Province.

Income-tax Act (XI of 1922), Secs. 22 (4), 23 (4), 30, proviso and 66 (2) and (3)—Estimate assessment under section 23 (4)—Assessee claiming to be non-resident of British India and hence not assessable—Appeal against

*(1928) I.L.R. 9 Lah. 464; A.I.R. (1928) Lah. 864.

assessment dismissed as not maintainable—Reference called on the claim of non-assessability and right of appeal.

The assessee in appealing against an assessment made under section 23 (4) for failure to comply with the terms of a notice under Sec. 22 (4) contended that he was not a resident of British India and hence was not assessable at all. The Assistant Commissioner dismissed the appeal as not maintainable and an application for a reference under Sec. 66 (2) was also rejected by the Commissioner.

On an application under Sec. 66 (3) the High Court directed the Commissioner to state a case on the two questions of law: (1) Was the Assistant Commissioner bound to decide whether the assessee was or was not a resident of British India; (2) Does the proviso to Sec. 30 bar an appeal on the question of liability to assessment when action has been ostensibly taken under Sec. 23 (4).

Application [Civil Miscellaneous Application No. 350 of 1926] made under section 66 (3) of the Indian Income-tax Act (XI of 1922) to direct the Commissioner of Income-tax, Punjab and North-West Frontier Province, to state a case for the opinion of the High Court.

G. C. Narang, for the Assessee.

Jagan Nath, for the Crown.

JUDGMENT.

HARRISON, J.—The Income-tax Officer of the Hazara Circle, in the North-West Frontier Province, in a considered order held that one Bhagat Duni Chand was a resident of British India and carried on business at Haripur in the Hazara district. He thereupon served him with a notice under section 22 (4) of the Act and, as he failed to comply with the terms of the notice, he made an assessment under section 23 (4) to the best of his judgment. From that assessment Bhagat Duni Chand appealed to the Assistant Commissioner and took the ground that he was not a resident of British India. The Assistant Commissioner, holding that no appeal lay from an assessment under section 23 (4), dismissed the appeal. The Commissioner, in his turn, dismissed the application for review and, holding that no point of law arose, refused to take action under section 66 (2) when asked to do so.

Before us it is urged that Bhagat Duni Chand was entitled to an adjudication by the Assistant Commissioner as to whether or not he is a resident of British India in the sense in which the words are used in the Act. Counsel for the Crown has relied on *Benarsi Das v. Commissioner of Income-tax* (1) but this ruling in our opinion does not advance the position at all. Granted that a man is an assessee and liable, therefore, to pay tax, and action is taken under section 23 (4), the matter is ended and he cannot challenge the correctness of the assessment or any other question incidental thereto. The question still remains whether he is or is not liable at all. We, therefore, direct the Commissioner to refer the question of law with his opinion thereon, the question being was the Assistant Commissioner bound to decide whether Bhagat Duni Chand was or was not a resident of British India, or does the proviso to section 30 bar an appeal on the question of liability to assessment when action has been ostensibly taken under section 23 (4).

[235] IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Justice Sir Cecil Walsh, Kt., K.C. and Mr. Justice Ashworth.

[15th February, 1928.]

Messrs. Chhitar Mal Ram Dayal

... *Assesseees.*

Income-tax Act (XI of 1922), Secs. 10 (2) (ix) and 66 (2)—Commission Agency business—Advances to Munims and Gumasthas written off as irrecoverable—Diwali presents to servants—Claim to deduct the two items as business expenditure—Rejection of claims by the Officer—Question, if one of law for reference to Court.

The assessee carrying on business on commission in various goods had advanced his Munims and Gumasthas certain sums of money which were written off as irrecoverable in the account year and claimed as business expenditure of that year under Sec. 10 (2) (ix). Another claim was made in respect of payments to his servants at the Diwali, the commencement of the business year. On the claims being rejected by the Income-tax Officer, the Commissioner on the assessee's application under Sec. 66(2) stated a case thereon to the High Court.

The High Court refused to issue notice on the case to the assessee, as the two questions raised were questions of fact determinable by the Income-tax authorities only.

Case [Miscellaneous Case No. 138 of 1928] stated under section 66 (2) of the Indian Income-tax Act by the Commissioner of Income-tax, United Provinces, for the opinion of the High Court.

CASE.

Messrs. Chhitar Mal Ram Dayal are a Hindu undivided family whose income is derived from property and from the business which they conduct as commission agents and dealers in grain, sugar and other commodities. The income which they returned in the current year was Rs. 5,486 for the accounting period Katik badi 15, S. 1982, to Katik badi 15, S. 1983, corresponding to November 1925 to November 1926. When their accounts were examined the Income-tax Officer disallowed certain items of expenditure on the ground that that had not been incurred solely for the purpose of earning the profits and gains of the business (section 10 (2) (ix) of the Income-tax Act). Among the items disallowed were two amounting to (i) Rs. 7,403, composed of sums of Rs. 5,220 and Rs. 2,183 due from the munib and the gomastha of the business, and (ii) Rs. 55 described in the books as Diwali expenses, on the ground that "the assessee has advanced large sums to his munims and other employees to meet their marriage expenses etc. These amounts were not recovered, but for what reason it is not possible to say. At any rate the assessee does not appear to have made any attempt at recovery. The item is clearly inadmissible.... Diwali expenses.... are inadmissible." The Assistant Commissioner upheld the view of the Income-tax Officer on appeal. The assessee now claims a reference to the High Court on the ground

"(i) That any amount which was actually advanced to the employees in previous years and written off in any subsequent year when the assessee thinks that the said amount is irrecoverable is a purely business deduction as

permissible bad debts under the provisions of the Indian Income-tax Act, XI of 1922.

(ii) That every customary expenses to any of the nature and which are an obligation to an assessee is a purely business deduction under Indian Income-tax Act, XI of 1922. Therefore the item of expenses at the time of closing up yearly accounts is purely business expenses and an admissible expense under the Indian Income-tax Act, XI of 1922."

A copy of the petition is attached (Appendix A*). The omitted portion relates to a point which the assessee has now withdrawn.

2. It is necessary to state the facts regarding the various items at some length. The sums written off as bad debts on account of advances to the munib and gomashta consist of the items given in the extract from the accounts for the three accounting periods shown in Appendix B.* It will be seen that the pay of the munib is Rs. 60 per mensem and the pay of the gomashta Rs. 50 per mensem. But as the accounts show and as was admitted before me by the representative of the assessee, the practice is for the proprietor of the business to make advances in cash and kind to his servants at various periods and in the case of one of the advances to the munib it is admitted that the advance was made on account of a marriage in his family. The idea of the assessee, as admitted before me, was to maintain a hold over the munib and gomashta by means of indebtedness to the owner of the business. And it will be observed that the assessee wrote off certain amounts which were not time barred at the time of the assessment and for which he could have sued for recovery through the civil court. It will be further observed that the assessee did not write off the whole of the outstanding amount in the case of the munib but left Rs. 1,136 outstanding. The amount due from the gomashta was written off in full. The assessee explains that he did not write off the total amount in the former case because he received jewellery valued at Rs. 1,136 from the munib and left the amount outstanding in order to give him an opportunity of redemption, but that he wrote off all the sum due from the gomashta because of a plea of inability to pay (*vide* copy of statement in Appendix C*). The assessee does not carry on a money-lending business although in the course of his general business he pays as well as receives interest on sums due from or to himself in the ordinary manner. He, therefore, did not make the advances to his servants as a money-lender and he further charged no interest on the outstanding amounts.

3. The Diwali expenses which were disallowed by the Income-tax Officer comprise the items shown in Appendix D.* It is clear that many of the items are in no way connected with the business, and before me the claim for set off was abandoned except as regards the sum of Rs. 33 which was paid to the servants of the firm on the occasion of the festival. These payments are a form of customary present on the occasion when the business year begins.

4. The questions of law which arise are as follows:—

(1) In the circumstances stated, were the advances made to the munib and gomashta of the firm expenditure incurred for the earning of profits and gains of the business?

(2) Was the expenditure on customary presents made to the servants of the business on the opening day of the business incurred to earn the profits and gains of the business?

5. The Commissioner is of opinion that, as the amounts were admittedly advanced to give the assessee a hold on his servants and as some of the loans were of a distinctly personal nature, *e.g.*, for a marriage as stated, the answer to the first question is in the negative. The answer to the second question in the Commissioner's opinion is also in the negative.

JUDGMENT.

We have come to the conclusion that the questions raised in the case submitted by the Commissioner cannot really be said to be questions of law. We think it better that we should give our reasons. This is the second case in which we have refused to issue notice. We did so the other day on what we thought questions of fact, explaining why, and expressing our view that the Commissioner was dealing very reasonably with assesseees by giving them every opportunity to obtain the opinion of the High Court, if it is at all legitimate to do so. We must, however, in the public interest discourage the notion that we sit under the Income-tax Act to decide cases stated by the Commissioner by way of appeal from findings of fact which do not satisfy the assesseees.

In this case the assessee claims that certain payments made to his Munib and Gomashta are payments incurred for the earning of his profits in his business within the meaning of section 10. The facts are these. The two employees are of course important men in the business of the assessee, who deals on commission in various goods. The assessee has lent money to his Munib and his Gomashta, as he says, for the purpose of keeping a hold upon them. One illustration of such loan was a loan to the Munib for marriage expenses. In one case the assessee went so far as to take security in the shape of jewellery from the Munib. The loans were made some years ago, and eventually the assessee had written them off as irrecoverable, and he claims to be allowed these sums as expenses of his business in the year in which they were written off. He put his original argument before the Commissioner in a quite absurd form. He stated they were bad debts. Clearly it is impossible to treat them either in fact, or in law, as bad debts of the business. Bad debt is a commercial term for trade debts, and cannot include loans made to your own servants, which are entirely private matters, independent of the business. We think it would be a legitimate view that these payments to servants were a trade expense under section 10, if the Commissioner really thought that they were in the nature of increments to salaries, such as perquisites, or food, which a man will supply to his servants in lieu of cash, but to make such perquisites, or payments part of the expense of the trade, they must be found by the Commissioner to have been made without any intention to reclaim them, and must be claimed as an expense in the year when they were made. In other words, it is a question of fact whether these apparent loans are really part of the wages, or rewards of the servants at the time when they were made. We are of opinion that this is a pure question of fact, and that the Income-tax Officer, the Assistant Commissioner or the Commissioner are the only tribunals to determine them in each case.

The other claim on which the assessee asks for a case to be stated as a point of law is a claim to take credit for certain Diwali expenses in the nature of payments to his servants at Diwali at the commencement of the business year. Here again it is a question of fact whether these payments are mere gifts, or acts of charity, or whether they can be reasonably found to be payments necessarily made by the assessee as part of his servants' wages in order to secure the services of his servants during the year of assessment in the trade or business. This is a question of fact, which must vary in each establishment according to the amount of the payment, the manner in which it is made, and the contract, if the Commissioner is satisfied that there is one, under which it becomes payable. If it is a mere gift, it is clearly not an expense in connection with the trade. The Commissioner must determine the question as a question of fact, and this Court has no right to attempt to lay down any directions as to how such questions ought to be decided. Under the circumstances, we think it right not to issue notice.

[236] IN THE COURT OF THE JUDICIAL COMMISSIONER, NAGPUR.

Before Mr. Findlay, Judicial Commissioner and Mr. Prideaux, Additional Judicial Commissioner.

[15th February, 1928.]

Messrs. Bansilal Abirchand, Rai Bahadur .. Assessee*

v.

The Commissioner of Income-tax, Central Provinces and Berar

.. Referring Officer.

Income-tax Act (XI of 1922), Sec. 13—Assessee engaged in several lines of business—Adoption of special method of account keeping—Accounts not closed and balance of profits and loss struck every year—Ascertainment of profit or loss only when transactions in a particular line cease—Assessments on this basis for a number of years—No notice by the Income-tax Department disapproving of the system—Right of the assessee to be assessed on his account keeping—Equitable estoppel.

The assessee carrying on business inter alia as a stock jobber and dealer in various commodities, had been adopting for a number of years a special method of keeping accounts. The accounts in respect of each line of business were not closed each year, striking the balance of profit or loss at the end of every year, but the figures were carried forward from year to year as book balances, the final gains or loss being ascertained at the end of the period when the transactions in that particular line of business cease. In the year 1925-26, the assessee who had been hitherto assessed on the basis of his special account keeping claimed a set off of about 6 lakhs of rupees shown in his accounts as losses in his stock jobbing and certain other businesses. The Income-tax authorities while accepting the assessee's account keeping basis when it showed a profit, rejected this claim on the ground that the assessee ought to have closed his accounts every year and that the sums claimed represented in reality the losses of the previous years when they ought to have been claimed.

* (1928) 24 N.L.R. 76; A.I.R. (1928) Nag. 102.

Held, that until the Income-tax authorities acting under the proviso to Sec. 13 issued specific orders disapproving of the assessee's system of account keeping as an unsuitable or improper one and directing the adoption of a different method of account keeping, the assessee was entitled to be assessed and to claim the set off for loss on the basis of his special method of account keeping.

Chengalvaroya Chetty v. Commissioner of Income-tax, Madras, 2 I.T.C. 14 and Subramanyam Chetty v. Commissioner of Income-tax, Madras, 2 I.T.C. 365, Referred to.

Case [Miscellaneous Judicial Case No. 60 of 1926] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Central Provinces and Berar, for the opinion of the High Court.

CASE.

Rai Bahadur Sir Bisessardas Daga, Kt., of Nagpur, proprietor of the firm of Rai Bahadur Bansilal Abirchand, who has business in several places in India including Burma, has put in an application under section 66 (2) of the Indian Income-tax Act requesting that reference be made to the High Court. He states as:—

1. The applicant has not been allowed the following deductions in arriving at his really taxable income:—

Serial No.	Rupees.	Nature of the item on which deduction was not allowed, though claimed by the assessee.	Reference to the Court's order in appeal No. 90 of 25-26 dated 4-6-26.
1.	5,01,200	Loss on New Great Eastern Mill shares.	Para. 2.
2.	48,831	Loss on account of the closure of the grain business at the Jubbulpore shop.	Para. 3.
3.	3,564	Do. do. in respect of Katni shop.	" 3.
4.	22,676	Loss in respect of the value of wheat of the Jubbulpore shop.	" 7.
5.	8,129	Dharmada receipts needlessly included in the income.	" 4.
6.	6,874	Prosecution charges.	" 5.
7.	32,191	Bad debts in respect of the business of the assessee's shops.	" 6.
8.	10,000	Combination expenses incurred by the business at the Madras shop.	" 10.
	6,33,465		

2. Was the Commissioner justified in disallowing the first three items mentioned in paragraph 1 on the ground that the assessee should have closed his accounts in respect of the aforesaid transactions every year, ascertained losses and claimed the same annually?

3. That the method of accounting regularly employed by the assessee being to incorporate in his head office accounts, only such accounts as are submitted from time to time by his several branches after a particular business therein gets closed on the final disposal of the entire commodity of that busi-

ness and it becomes possible to strike the profit and loss account thereof, was not the Commissioner bound to hold:—

(i) that the losses claimed above appertained to the year when they were incorporated in the head office accounts, and

(ii) that the assessee was as a matter of right entitled to set them off against the gross profits, to ascertain his taxable income?

4. That since as a matter of fact no yearly accounts of profits and losses were made of the aforesaid transactions and that the accounts were in fact made in the year Sambat 1980-81, was not the Commissioner bound to hold that the aforesaid losses appertained to the 'previous year' for which the return was submitted?

5. In view of the fact that the winding up of the shops at Jubbulpore and Katni had proceeded up to a date that actually fell in the year Sambat 1980-81 though the shops stopped doing actual trade in 1979-80, was not the assessee within his rights in ascertaining his actual loss at the end of the winding up and claiming the same in accounting year?

6. Was the Commissioner warranted in disallowing the loss on hypothesis that the loss, if any, to the assessee must be held to have occurred as soon as his shops stopped trading or doing business in 1979-80 and that the loss so suffered could not be set off against the income arising in the Sambat year 1980-81?

7. Was the Commissioner justified in assessing the value of the stock of wheat bags at the Jubbulpore shop admittedly purchased in 1979-80 or in previous years, at a rate of Rs. 20 per bag, at the market value of each such bag at the opening of the previous year of 1980-81 and thus under-value the price of the said opening stock by holding that each bag was then only worth Rs. 10 as per that market value?

8. Is the Commissioner warranted in ruling that the money actually spent in the purchase was not the point and that the assessee was bound to find out and carry forward to the year 1980-81 the loss on these wheat bags on finding their worth at the end of the year 1979-80?

9. Is the Crown warranted in resisting the claim of the assessee for the recognition of the loss on the said wheat stock to the extent of Rs. 22,676 on the ground that the loss that could be found out on adopting process of accounting suggested in the above ground should have been deducted in showing the income in the return for the Sambat 1979-80?

10. In view of the undisputed fact that the assessee holds in trust for charities the Dharmada Fund the receipts of which in the year of accounting were Rs. 8,129, is he not entitled to claim that these receipts should not be deemed to be a part of his taxable income according to the principles of section 4, clause (3) of the Indian Income-tax Act?

11. Was the Commissioner warranted in holding without any evidence that the Dharmada Fund admittedly set apart for several generations by the assessee's firm and utilised for the purposes of charities that "it is merely a matter of convenience that the firm sets apart certain capital but the nature of the transaction is only personal because nobody can compel him to spend the money in a particular way"?

12. That since the accounts of the assessee were held to have been kept on the mercantile system and since the account books were duly examined by

the Income-tax authorities who actually found that the items aggregating to Rs. 32,191 were definitely written off as irrecoverable bad debts, were the Income-tax authorities justified, either under the Indian Income-tax Act or the rules made thereunder, in demanding from the assessee further information in regard to the history of these debts?

13. Was the Commissioner warranted in ignoring at the stage of the judgment the information of the bad debts supplied by the assessee in a list which was filed along with the appeal memo. on the ground that the same was not signed and verified?

14. Assuming that signing and verification was necessary, was the Commissioner not bound to return the same for amendment with a view to get the technical flaw set right, especially when he heard the assessee's agent at four hearings and disoused on the merits of that written information?

15. Was the Commissioner right in holding without any evidence that 'the debts are so old that the amount had become irrecoverable long ago'?

16. In view of the fact that the assessee did not deem it necessary by any circumstances to consider these outstandings as bad debts till the time when he wrote them off on their appearing to be irrecoverable as the account books would show, is the Commissioner warranted in holding that these debts deserved to be considered as losses the moment they became more than three years old and could not be recovered in a court of law in view of the law of limitation of British India?

17. Is not the assessee entitled to treat the prosecution charges of Rs. 6,874 as a business expenditure, in view of the fact that these prosecutions were indisputably undertaken for tracing the property of the assessee's shop and incidentally for bringing the offender to justice?

18. Is not the assessee warranted in claiming the combination charges of Rs. 10,000 as an expenditure necessary for commanding greater facilities and better business touch, with a view to gain higher profits as well as to keep down losses with the assistance and good-will of the other traders in the Madras market?

I refer the points of law mentioned herein for the decision of the learned Judges of the High Court excepting those referring to items Rs. 6,874 and Rs. 32,191 (which are allowed by me by taking the case on my revision file) and to item Rs. 10,000 which, as I shall show, is based on a question of fact.

II. FACTS OF THE CASE.

I would first like to give the facts of the case as briefly as I can. The applicant closes his accounts on Diwali day. On his accounts for Sambat 1979-80 he was assessed on an income of Rs. 14,12,943. For assessment during the year 1925-26 he made a return of a loss of Rs. 13,92,272 based on his account for the year Samvat 1980-81, i.e., ending in Diwali 1924. Return being not accepted, accounts were looked into and among other items disallowed were the ones mentioned in para. 1 of the application for reference.

Item Rs. 5,01,200.—The applicant has some dealings in share market transacted at his Bombay branch. He had been purchasing and selling shares of several companies and therefore calls himself a stock-jobber. He started purchasing shares of the New Great Eastern Mill in Samvat 1977-78 and this business has been continued till Samvat 1980-81. In this interim shares had

been purchased and sold and though accounts of each Samvat are recorded separately, the balances are never struck at the end of every Samvat. In Samvat 1980-81 the accounts are said to have been finally closed because not one share of this company remained with the applicant. He claimed a loss of Rs. 5,96,668. But as this loss was sustained in transactions taking place over as many as four years it was not allowed. Rs. 95,468 on account of interest charged on capital was allowed as it was accounted for elsewhere, and the net loss of Rs. 5,01,200 was disallowed. If accounts of the "previous year" only (Samvat 1980-81) were to be looked into, there was an actual profit of Rs. 24,314 over the transactions taking place in this year. But my predecessor in his order of appeal, dated the 4th June 1926 owing to his leniency did not take this into consideration and simply disallowed the loss in question after observing that the accounts of the "previous year" only were to be taken into consideration. The total disallowance should have been Rs. 5,25,514.

Items Rs. 48,831 and Rs. 3,564.—The grain shops at Jubbulpore and Katni under the applicant's branch at Jubbulpore were started more than ten years ago. They were closed at the end of Samvat 1979-80 because, as explained, no profit was obtained out of them. There was no grain left in these shops. If there was any loss on them it should have been returned and claimed in the assessment of 1924-25 based on the accounts of the year Samvat 1979-80. The applicant's contention is that the accounts were not settled because the Munim had died and because some debts remained to be collected. He says that the accounts were settled finally in Samvat 1980-81 and therefore they are claimed as accruing in that year. The two losses occurred in the shops at Jubbulpore and Katni, respectively.

Item Rs. 22,676.—At the Jubbulpore shop 2,227 bags of grain had been lying from years before. There had been no transactions in these during the year Samvat 1980-81. The applicant valued the opening stock at Rs. 20 per bag, i.e., at the purchase price paid years ago. The valuation by my predecessor was made at Rs. 10 per bag which was the price prevalent at the beginning of the account year (previous year). Hence the difference, i.e., Rs. 22,676 was disallowed. It seems the assessee is seeking to carry forward losses from one year to another (or to be assessed on a balance of several years' profits and losses) which the Income-tax Act does not permit. In this case the profit or loss in each year should have been ascertained by valuing closing stocks at the market price or the cost price whichever was less and by this method only could the profit and loss of each year be ascertained and allowed or disallowed in that year. The value of the closing stock in one year should have been carried forward as the value of the opening stock in the next year. The profit or loss in each year with which the Income-tax Department is concerned can only be the difference between the value of the opening stock in that year and the price at which it was sold.

Item Rs. 8,129.—This item consists of as many as 11 items referring to 11 different shops. It is shown as interest paid on amounts set apart by applicant's predecessors for charitable purposes and that it is utilised for such objects only. It seems as if it was a matter of convenience that this arrangement has been ordered at the different shops and that such items are shown as interest on the capital invested for charitable purpose. After all, the applicant himself is the owner of the money. He has created no trust in it, nor can anybody

compel him to spend the money in any particular way and as such the items claimed as interest paid on investments were disallowed.

Item Rs. 10,000.—This was the amount alleged to have been paid to money-lending Marwaris of Madras where the applicant has a branch, with the object of keeping the rate of interest on loans made, as high as possible. It is alleged that the Marwaris had formed an association with this object and that this amount was paid to them. It is therefore claimed as a business expenditure because higher rate of interest was expected to be obtained. My predecessor disallowed this expenditure for the reason "unless we know exactly what was the object of this payment and how it was actually spent bringing in higher profits, we cannot accept this payment". It is, therefore, a question of fact whether such an expenditure was really met to gain higher profits or not and as this was not proved the expenditure could not be allowed.

III. OPINION.

Para. 2 of the application.—I beg to think that the disallowance of the first three items mentioned in paragraph 1 of the application for reference has been correctly made because of the law requiring the tax to be levied "on profits and gains of the previous year only" (section 3 of the Income-tax Act). The assessee cannot be allowed on the excuse of his accounts remaining unsettled for number of years, to claim assessment on the average income made on the whole transaction; for that would mean taxing him on the averages of incomes and losses of that period. The law requires each year's income or loss to be taken into account.

Para. 3 of the application.—(i) The losses claimed could not be held to appertain to the year when they were incorporated in the so-called head office accounts, for they did not actually appertain to that year as shown above. In the account year, Samvat 1980-81, there was a gain in the share-market transactions and no loss in the grain shops at Jubbulpore or Katni. The losses referred to the previous years and could not therefore be allowed in the account year.

(ii) For reasons given above the assessee could not set off this loss against his other taxable income.

Para. 4 of the application.—This question seems a repetition of what is said above and, for reasons given above, I submit that this issue also requires to be answered in the negative.

Para. 5 of the application.—An assessee must render accounts of each year separately. He may wind up his business any time he likes but the gains or losses of each year have to be taken into account in that year, and, as admitted by applicant, the Katni and Jubbulpore shops closed for business purposes before Samvat 1979-80. There was no loss incurred in these shops after that. No such loss therefore could be allowed in the accounts of Samvat 1980-81.

Para. 6 of the application.—For this too I have given my opinion above.

Para. 7 of the application.—The question does not definitely make mention of the facts. The words "purchased in 1979-80 or in previous years" leave very much in doubt as to the year in which bags numbering 2,227 were purchased. They were not purchased in Samvat 1979-80 but they were purchased in 1978-79 and as such they had already been over a year old on the first day of the "previous year", Samvat 1980-81. If they were purchased at Rs. 20 per bag two years

before, surely their value had depreciated in the year preceding the "previous year" and on the first day of the "previous year" their value should have been taken to be the one prevalent on that date which has been authoritatively found to be Rs. 10 per bag. The valuation made by the Department was therefore correct for the purposes of finding out the profit or loss of the year in question.

Para. 8 of the application.—I have given my arguments against this issue above and would beg to repeat that from each year's accounts profits and gains have to be found out and to that end valuation of stock every year is necessary.

Para. 9 of the application.—My reasons for this too are given in para. 8 above.

Para. 10 of the application.—It is denied that the applicant holds in trust for charities, the Dharmada fund. It is the applicant's own doing and therefore it cannot be called a trust, nor is its income exempt under section 4 (3) (i) of the Income-tax Act.

Para. 11 of the application.—I beg to submit that the finding given in this respect by my predecessor seems correct.

Paras. 12 to 17.—Not referred as these items Rs. 32,191 and Rs. 6,874 have been allowed in revision.

Para. 18 of the application.—It was a question of fact as to whether the amount in question was or was not spent to gain higher profits as well as to keep down the loss with the assistance and good-will of other traders in the Madras market and as the applicant has failed to prove this he cannot ask for a reference on this point.

G. L. Subhedar and P. R. Srinivasan, for the Assessee.

Rai Bahadur D. N. Choudhari, for the Crown.

JUDGMENT.

1. This is a reference by the Commissioner of Income-tax under section 66 of the Indian Income-tax Act, the non-applicant being the firm of Messrs. Bansilal Abirchand, R. B. Bankers, the managing proprietor of which is Rai Bahadur Sir Bisessardas Daga.

2. The non-applicant has been assessed to income-tax for the year 1925-26. His income-tax in certain respects has been assessed on the profits of the previous year. The non-applicant firm owns branches both in and outside the Province and indulges in various kinds of business, besides that of banking proper. The firm owns considerable property at various places and shares in a number of permanent partnerships and the like.

3. Five questions have been referred for our opinion:

(i) Whether the loss of Rs. 5,01,200 said to have been incurred on New Great Eastern Mill shares and claimed in the year under assessment should have been allowed to the non-applicant;

(ii) Whether the loss of Rs. 48,831 on account of the closure of the grain business at the Jubbulpore shop should have been similarly allowed to the non-applicant;

(iii) Whether a similar loss of Rs. 3,564 in respect of the Katni shop should have been allowed to the non-applicant;

(iv) Whether a loss of Rs. 22,676 in respect of the value of the wheat of the Jubbulpore shop should have been allowed to the non-applicant; and

(v) Whether *Dharmada* receipts amounting to Rs. 8,129 were improperly included in the income of the non-applicant.

4. The first three questions mentioned above admittedly stand or fall together, the same principle being involved in connection with the question of whether or not these losses could be properly claimed by the non-applicant in the year under assessment. In paragraph 2 of the Assistant Commissioner's report of the 15th February 1926 a fair enough description is given of the method adopted by the non-applicant in connection with the items we have mentioned above. In the case of stock jobbing business and the like it has apparently been the practice of the non-applicant to adopt a somewhat special method of keeping accounts. There are two such obvious methods: one to spread the profits or losses over the whole term of years in which transactions occurred, or to take final losses or gains at the end of the period when the transactions completely cease.

5. In the case of the New Great Eastern Mill shares the non-applicant adopted the latter method. From 1977 onwards up to the year preceding assessment the non-applicant had been dealing comparatively largely in these shares. Transactions both of buying and selling had taken place but in the year on which the non-applicant's income is based he remained without a single one of these shares in his possession. For the first time, therefore, then, the total loss involved in the dealings as regards these shares was claimed by the non-applicant as a set off for the purposes of income-tax assessment.

6. The Assistant Commissioner of Income-tax in paragraph 2 of his order, dated the 15th February 1926, was of opinion that the non-applicant should have closed his share account during each of the years in which transactions in this Mill shares took place. He pointed out that the fact of the non-applicant hoarding up his account of these shares for several years was apparently inconsistent with the principle underlying section 3 of the Income-tax Act. The Assistant Commissioner's argument in this connection may be put in a nut-shell as follows:—

"The assessee did not close his accounts annually, but carried the whole thing as a book balance and accumulated the loss of three or more years in this year's account. This is not allowable by the Income-tax Law, as his accounts ought to be closed every year and the loss should be claimed every year."

7. The Commissioner of Income-tax in dealing with the assessee's appeal was also of opinion that the method of account adopted by the latter was not permissible. He held that the loss on these shares claimed by the assessee could not be regarded as the loss of the previous year but represented in reality the loss of various previous years in which the book balances had simply been carried forward without any actual striking of a profit or loss in any of the intervening years.

8. The guiding provision of law in this connection is to be found in section 13 of the Income-tax Act. That section lays down that "income, profits and gains shall be computed in accordance with the method of accounting regularly employed by the assessee: provided that if no method of accounting has been regularly employed, or if the method employed is such that, in the opinion of the Income-tax Officer, the income, profits and gains cannot pro-

perly be deduced therefrom, then the computation shall be made upon such basis and in such manner as the Income-tax Officer may determine."

9. Turning to paragraph 35 of the Instructions regarding the Income-tax Law and rules to be found at page 97 of the Income-tax Manual, the possibility of assessing the non-applicant in accordance with the system of account he has adopted, is clearly adumbrated in the last sentence of the 1st paragraph of Instruction No. 36. For our own part, we are wholly unable to see why the non-applicant should not be allowed to claim the losses in question under the system of account adopted by him. If that system of account is considered by the Income-tax Officer as an unsuitable or an improper one, he can issue specific orders in the matter under the proviso to section 13, but until he has done so, we are of opinion that the system of account adopted by the non-applicant should, in the meanwhile, have been accepted for the purpose of assessment of income-tax in the year under assessment. It seems obvious that whether the book system of account adopted by the non-applicant is a desirable one or not, no profits can eventually escape taxation thereunder, although possibly the Income-tax authorities might in any particular case have to wait a long time before receiving profits. Curiously enough, the Income-tax Commissioner, in his order dismissing the non-applicant's appeal, has, to all intents and purposes, admitted that in connection with these shares the non-applicant must have incurred losses in previous years—losses which were admittedly not allowed for. In the year under assessment the Income-tax Commissioner calculates that there was an actual gain of over 24,000 rupees as regards the dealings in these shares, but he with a generosity, which is perhaps unusual in the case of Income-tax authorities, did not take this profit into account for the simple reason that he could not at that time of day allow the non-applicant for the losses in the previous years.

10. A very pertinent circumstance in connection with the question we have to decide is the fact that the non-applicant has, in at least two cases, *e.g.*, the Birla Jute Mills and the Hukumchand Mills, been admittedly taxed on petty profits derived from these shares in the preceding years—profits which were arrived at on precisely the same system of accounting which is now objected to by the Commissioner of Income-tax. In the case of these shares, the account was similarly finally struck after the last batch of shares had been disposed of, and the net profit as shown in the year, on the basis of which the assessment of income-tax was made, was included in the non-applicant's income for the purpose of assessment. It has been urged on behalf of the non-applicant that the proper procedure for the Commissioner was, under the proviso to section 13 of the Income-tax Act, to have given the non-applicant due notice that, in his opinion, the income could not be properly deduced from the method of accounting employed and that a different method of accounting would have to be adopted. It has been urged in this connection that a question of estoppel arises and, while we are of opinion that there is no question of the doctrine of estoppel as a mere rule of evidence applying, it does seem to us that the doctrine of equitable estoppel necessarily arises in the circumstances of the case. The Commissioner of Income-tax has for other purposes, *viz.*, the Hukumchand Mills and Birla Jute Mills, accepted, for purposes of estimation of profits, precisely the same system of accounting which he now objects to when, as in the case of New Great Eastern Mill shares, a loss has occurred. This position seems to us contrary to the most elementary principles of justice and equity and, in reality,

amounts to saying that an assessee's income in any given year is what he has made out of a profitable branch of business but that, at the same time, any loss made in another absolutely analogous branch of his business should not be taken into account in determining what his assessable income is.

11. We see, moreover, that considerable difficulty is likely to arise in the method of accounting which the Commissioner of Income-tax considers should have been adopted by the assessee. He apparently desires the assessee in each year to estimate his losses on the stock of shares in question. Any such system, it seems to us, might prove a highly unsatisfactory one. The market prices of shares on the stock-exchange vary immensely even from day to day and any such system based on the idea of arbitrarily closing accounts on a certain date might prove a highly artificial and unsatisfactory one. Under the applicant's system of keeping account, assuming it to be carried out in a business like, thorough and straightforward fashion, it seems to us inevitable that actual losses or gains as regards the stock or shares in question over the whole set of transactions connected therewith will be definitely known when the transactions in these have ceased for good and all. Indeed, from another point of view, it would seem impossible in any given year in the case of shares like these to arrive at any reasonable or proper estimate of profit or loss incurred for the simple reason that it is impossible to estimate at their proper value whatever shares concerned the holder may still have in his hands. We have already alluded to the fact that the Commissioner of Income-tax estimated that a profit of Rs. 24,000 odd had been made on these shares in the *Sambat* year 1977-78, but this estimate seems to us a purely artificial one for the simple reason that, in appraising the shares on hand, the Commissioner of Income-tax took their value at the price of the last transaction which occurred therein. Under the conditions then prevailing as regards such shares, any such value might be artificial and very far from the truth, and the method adopted is an extremely arbitrary one. Unless and until, therefore, the Commissioner of Income-tax sees cause to insist under section 13 of the Indian Income-tax Act on the assessee employing another method of accounting, we are of opinion that, having regard to the provisions of section 24 of the Indian Income-tax Act, the assessee was entitled to claim a debit for the loss incurred on these New Great Eastern Mill shares. As we have pointed out, it is clear that in connection with other shares the Commissioner accepted this method for the purpose of calculation of gains, and the principle laid down by Coutts Trotter, C. J., and Krishnan, J., in *Chengalvaraya Chetti v. Commissioner of Income-tax, Madras*,⁽¹⁾ seems to us to be fully applicable to the present case: *cf.* also *Subramaniam Chettiar v. Commissioner of Income-tax, Madras*⁽²⁾. We would, therefore, answer the first question referred to us in the affirmative.

12. Coming to the second question, *e.g.*, the loss of Rs. 48,831 incurred on account of the closure of the grain business at the Jubbulpore shop, precisely the same considerations apply and the same remark applies to the loss of Rs. 3,564 in respect of the Katni shop.

13. The fourth question referred for decision is whether the loss of Rs. 22,676 incurred in connection with the value of bags of wheat at the Jubbulpore shop should have been allowed. At the beginning of the account year the

(1) 2 I.T.C. 14.

(2) 2 I.T.C. 365.

non-applicant found himself with 2,227 bags on hand and took credit for these at the actual price he had paid for them, *viz.*, Rs. 20 a bag. The Commissioner of Income-tax, however, only allows Rs. 10 a bag, as he finds that in the year in question that was their actual market value. If the Commissioner of Income-tax is correct in his estimate of the value it follows that, in the preceding year or the previous one, the non-applicant must have incurred a loss of Rs. 10 per bag in connection with the said stock. Admittedly, this was never claimed and, as the assessee had in previous years neither showed profits nor claimed losses on this stock, we are of opinion that every consideration of justice and equity required that the stock should be valued at the original price paid by the assessee for it, if we are to arrive at a really correct and not an arbitrary calculation of his profits or losses in connection with this branch of the business. It is not disputed that the same system of accounting was, *mutatis mutandis*, adopted in connection with this item as applied in the case of the first three items we have dealt with above and for the same reasons we would answer the fourth question referred to us in the affirmative.

14. The fifth question stands on a different footing. The suggestion on behalf of the non-applicant is—*vide* the statement of his agent made on 30—7—26 that these *Dharmada* receipts really refer to a trust fund and should be excluded from the income. The item in question is made up of 11 items referring to 11 different shops. It is shown as interest paid on amounts set apart by the non-applicant's predecessors for charitable purposes and it is alleged that it is only used for such purposes. We are wholly unable to see that real elements of trust are present therein. Very obviously, the non-applicant can, by an oral or a written order at any moment, completely alter the nature of this fund and can, in short, abolish the *Dharmada* system if he so desires. The management, its nature and the distribution of the proceeds are entirely within his own volition and no one can compel him to spend the money in any particular way. We agree with the Commissioner of Income-tax that this amount has been properly included in the income. We, therefore, answer the first four questions referred to us in the affirmative and the fifth question in the negative. In other words, as regards the fifth question the *Dharmada* receipts amounting to Rs. 8,129 were properly included in the income of the non-applicant.

15. As regards costs, the non-applicant has succeeded in the main and we accordingly order the applicant to bear his costs which we assess at Rs. 250.

[237] IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Mr. Justice Harrison and Mr. Justice Dalip Singh.

[21st February, 1928.]

Mohamad Farid-Mohamad Shafi

.. Assessee*

v.

The Commissioner of Income-tax, Punjab and N.W. Frontier Province.

Income-tax Act (XI of 1922), Secs. 33 and 66 (1), (2) and (3)—Assessment by Commissioner under Sec. 33—Application to High Court, for re-

ference rejected as not maintainable—Issue of demand notices wrongly headed under Sec. 29—Subsequent application to High Court for reference—If competent.

In respect of an assessment made by the Commissioner of Income-tax under Sec. 33 of the Act, the assessee after unsuccessfully applying to the Commissioner under Sec. 66 (1), moved the High Court for a reference and the Court rejected the same as not maintainable. Subsequently on the issue of a demand for tax by the Income-tax Officer headed as under Sec. 29 describing the assessment as falling under Secs. 23 and 33, the assessee again applied to the Commissioner for a reference on the legality of the demand as well as on other points already rejected. The Commissioner agreeing with the assessee that Sec. 45 and not Sec. 29 applied to the case offered to return the reference fee and refused a reference on the other points.

On an application to the High Court for an order directing the Commissioner to state a case on the other points.

Held, that the error of the Income-tax Officer in quoting Sec. 29 would not give any special jurisdiction to reagitate the points previously raised and refused to be referred.

Application [Civil Miscellaneous Application No. 451 of 1927] under section 66 (3) of the Indian Income-tax Act (XI of 1922) for an order directing the Commissioner of Income-tax, Punjab and N. W. Frontier Province, to state a case for the opinion of the High Court.

J. G. Sethi, for the Assessee.

Jaggan Nath Aggarwal, for the Crown.

JUDGMENT.

Acting under section 33, Income-tax Act, the Commissioner assessed the present petitioner to an additional sum of Rs. 6,000 odd. The petitioner presented an application under section 66 (1) asking to have certain points of law, which he alleged arose, referred to the High Court. On the Commissioner declining to take action, an application was made to this Court which was rejected by a Division Bench, an order* being passed to the effect that whatever power the Presidency High Courts might have of compelling a reference under section 66 (1), this High Court had no such power and as the action taken by the Commissioner was taken under section 33, no relief could be given. After this decision had been announced a notice of demand was issued by the Income-tax Officer to the petitioner for the recovery of the amount so assessed. This was described and headed as under section 29 and the assessment was described as falling under sections 23 and 33, the decision having been under section 33. On receiving this demand the petitioner paid the money and then applied to the Commissioner to refer not only the question of the legality of the demand but also all the other points which he had unsuccessfully attempted to agitate before. The Commissioner gave a finding that section 29 did not apply and had wrongly been referred to by the Income-tax Officer. He pointed out that action should have been taken under Ch. VI and referred to section 45. He then offered to return the deposit as he had decided the only point involved in favour of the petitioner.

*Reported as 2 I.T.C. 430.

The petitioner has now come to this Court again and contends that because section 29 was wrongly invoked and wrongly quoted by the Income-tax Officer, the door is somehow opened which was formerly closed, and he is entitled to agitate all the points contended on the previous unsuccessful application, and this because the error committed by the Income-tax Officer in some curious way creates a new and special jurisdiction under section 66 (1) to deal with points which normally could only reach this Court if referred under section 66 (1), inasmuch as they arise out of an order passed by the Commissioner under section 33.

We are of opinion that the decision of the Commissioner was right and that section 29 was wrongly used. As we agree with him, there is no question of our granting leave to refer the question on which we do agree. We are of opinion that the other points cannot be agitated now, any more than they could be agitated before and that no special jurisdiction has been created by the error of the Income-tax Officer in quoting section 29.

We, therefore, dismiss the application. No order as to costs, as Rs. 100 have been deposited and not repaid.

[238] IN THE HIGH COURT OF JUDICATURE AT LAHORE

Before Mr. Justice Harrison and Mr. Justice Dalip Singh.

[21st-February, 1928.]

Messrs. Rattan Chand Dunichand of Guru Bazar, Amritsar .. *Assessee*
v.

The Commissioner of Income-tax, Punjab and N.W. Frontier
Province .. *Referring Officer.*

Income-tax Act (XI of 1922), Secs. 22 (2) and 23 (4)—Return form sent with columns not filled—"Blank" written against "total" column—Covering letter disputing assessability—If a valid return—Assessment under Sec. 23 (4), validity of.

Where an assessee served with a notice under Sec. 22 (2) of the Act returned the form signed, without any date, with all the various columns left blank, with the word "blank" written against the item "total" and accompanied by a covering letter in which it was explained that no business was carried on in Amritsar,

Held, that the assessee was assessable under the provisions of Sec. 23 (4) as having failed to make a return.

Case [Case No. 34 of 1927] stated under section 66 (3) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, Punjab and N. W. Frontier Province in compliance with the order of the High Court dated 23rd June 1927.

CASE.

By an order of the High Court (Mr. Justice Broadway Ag. C. J., and Mr. Justice Bhide) dated the 23rd June 1927, I am required to state a case on

a question of law arising out of the facts given in paragraph 1 of the order, which, for convenience of reference, I reproduce *in extenso*.

"The firm of Messrs. Rattanchand Dunichand have certain premises in the Guru Bazar in Amritsar. They have also business in Kashmir. They were served with a notice under section 22 (2) of the Income-tax Act, calling upon them to furnish a return of their incomes. They signed a prescribed form, and refraining from making any entries in the various columns, wrote the word 'blank' against the item 'total'. This return was sent by them to the Income-tax Officer with a covering letter, in which it was explained that they carried on no business in Amritsar and received no income at that place, and that the writing of the word 'blank' on the prescribed form meant that the firm in Amritsar had no income of any kind whatsoever. The Income-tax Officer then issued a notice to this firm under sub-clause (4) of section 22, calling upon them to produce all their accounts in connection with their business. This notice was issued on the 15th of August 1925, but was not served. A similar notice was issued on the 9th of September 1925, but was served on a wrong person with the result that another one had to be issued on the 12th September 1925, of which service was duly effected. A member of the firm appeared before the Income-tax Officer, and there made certain statements to the effect that they kept no accounts of any dealings they might have had in Amritsar and that the main accounts in any case were in Kashmir. After further time had been given by the Income-tax Officer, (and it may be that another notice was issued calling for account books regarding which there is some question,) the Income-tax Officer treated the case as a "no return case" and made the assessment under section 23 (4). This assessment was appealed against and ultimately taken up to the Income-tax Commissioner who was asked either to review the proceedings, or under the provisions of section 66 (2) of the Income-tax Act, refer certain questions of law to this Court. The Income-tax Commissioner held that there was no question of law involved which could be referred to this Court, with the result that Messrs. Rattanchand Dunichand have moved this Court for a mandamus under the 3rd clause of section 66".

2. The question that I am required to refer is:—

"Whether a 'return' such as was made in this case, namely, the signing of a prescribed form without any date, with all the various columns left blank and the word 'blank' written against the item 'total', accompanied by a covering letter such as has been referred to above, is "no return" for the purposes of assessment under section 23 (4)".

3. The return in question was furnished under section 22 (2) of the Income-tax Act, which states that it should be "in the prescribed form and verified in the prescribed manner" and set forth the assessee's "total income during the previous year". The return is blank except for (a) the word 'blank' written on para 1 against the heading "total income", and (b) the declaration on the same page being signed. The declaration is not dated and does not state the year to which it relates. All, therefore, that was declared was the name of the declarer and the fact that, for some unspecified period, the declarer's income was "blank". In a covering letter it was explained that a blank return was sent "on the reason that firm named Rattanchand Dunichand at Amritsar (i.e. the petitioners) is a branch of the firm named Rattanchand Rakhamal at Kashmir", and it was added that the 'duty' of the Amritsar busi-

ness was "to purchase goods and send to Kashmir for sale, where profit on goods is earned in the regular course of business. Further duty of this firm is to pay off debts, and do nothing else. i.e., no sale business is carried out here".

Finally, after explaining the "duties" of the Amritsar business, the letter concluded by challenging the validity of the notice issued under section 22 (2) and by offering to submit any further information required. As to this offer, it may be noted that, inspite of notices under section 22 (4), the petitioners subsequently refused to produce the accounts of either their Kashmir business, or of certain brokerage done by them at Amritsar. It is also to be noted that the letter does not state to what year the return relates; nor does it give any of the particulars required by the return. The first omission is, by no means, unimportant, as it might invalidate a prosecution under section 52 of the Act. Even, therefore, if the letter is regarded as an integral part of the return, the particulars required by section 22 (2) were not furnished.

4. That these particulars might have been furnished, is clear from the petitioners' application, dated the 17th March 1926, under section 33 of the Act. Paragraph 2 of this application gives a detailed profit and loss account of the business done at Amritsar. This account includes the following items:—

(a) Rs. 2,085-3-3, received by the Amritsar business by way of $1\frac{1}{2}$ per cent. commission on the goods supplied from Amritsar, and

(b) Rs. 200, an estimated figure of the brokerage income of L. Duni Chand.

These items clearly constitute income and should have been entered in the return. The annual value of a residential house at Amritsar, in which the petitioners admittedly had a share, should also have been declared in accordance with note 4 in the return. Similarly, figures should have been given for the whole business done at Amritsar, as required by note 5, for the business was done in British India, and any profit arising from it was liable to taxation under section 4 (1) of the Act. If it is contended that no profit arose from the business, the necessary figures should still have been given to enable the Income-tax Officer to judge whether the business was done at a profit or at a loss, or whether, owing to the special circumstances, neither profit nor loss arose or accrued in British India.

5. The omission of one of these items might possibly not have invalidated the return, but the omission of them all is tantamount to submitting no return at all. It is definitely stated in section 22 (2) of the Act, that the return must be "verified in the prescribed manner", and set forth "total income during the previous year." For a return to be valid in the prescribed manner, it must state the year to which it relates, and for total income to be set forth, clearly some figure must be given when business is done. In this case, on the petitioners' own showing, business was done amounting to nearly a lakh but no figures were given in either the return or the covering letter, and the return itself did not state to what year it related. The Income-tax Officer, therefore, had no alternative but to make the assessment under section 23 (4), which applies when a person "fails to make a return under..... sub-section (2) of section 22". I consider, therefore, that the question stated for reference should be answered in the affirmative. Even if it is answered

in the negative, it is doubtful whether the petitioners will benefit, as the assessment was made under section 23 (4), not only because they failed to make a return, but also because, as stated above, they failed to comply with the notice issued under section 22 (4) for the production of the Kashmir and brokerage accounts.

6. A copy of this reference was sent to the petitioners. In two letters dated the 13th August and the 19th September, they asked that certain additions should be made. This I have declined to do, as none of them seemed to me to touch any relevant question of fact. I attach a copy of the correspondence in case it is desired to refer to it.

Mehr Chand Mahajan, for the Assesseees.

Lala Jagan Nath Aggarwal, for the Crown.

JUDGMENT.

The question referred to by the Income-tax Commissioner is as follows:—

Whether a 'return' such as was made in this case, namely, the signing of a prescribed form without any date, with all the various columns left blank and the word 'blank' written against the item 'total', accompanied by a covering letter in which it was explained that the firm in question carried on no business in Amritsar, is 'no return' for the purposes of assessment under section 23 (4)?

Section 22 (1) says that "the principal officer of every company shall prepare a return, in the prescribed form, which is sent to him by the Income-tax authorities and verified in the prescribed manner, of the total income of the company during the previous year".

Counsel contends that, in the first place, the word 'blank' must be read as having a totally different meaning from that to be found in the dictionary, that it means 'nil', that the absence of the date is wholly immaterial as it is the business of the Income-tax department to look up the register and other papers and find out the year referred to in the notices and fill up the *lacunae*, that the signature on the form together with the verification somehow supplied the missing details and made the form no longer a blank form, but one sufficiently filled up to be a "return". The word "blank" is explained in the Oxford Dictionary as "not written or printed on (of paper) (of document) with space left for signature or details". Blankness is the negation of any entry and how that which is blank can be said to constitute a "return" containing all or any necessary facts, figures and details, appears to us impossible to understand. In our opinion this form was, what it said it was, a blank form and the writing of the word 'blank' merely emphasized and drew attention to the fact that nothing had been shown in any column and that the verification was meaningless as verifying nothing at all. But counsel urges, the covering letter must be read with this blank form and, if the necessary figures are to be found in that covering letter, it may be said that the necessary return has been made in the prescribed form, the information there called for having been supplied. Even if the view were accepted we find that the covering letter does not supply the information, let alone supplying it in the prescribed form. It merely challenges the rights of the Income-tax Officer to call for a return at all and does

not say that the addressee had no assessable income. Even if we read the two together, therefore, as counsel would have us do, we find that there had been no return in the prescribed form and that the action taken by the Income-tax Officer was quite correct.

We answer the question accordingly and hold that there has been no return. No order as to costs; Rs. 100 have already been deposited by the unsuccessful petitioner and have not been returned.

[239] IN THE HIGH COURT OF JUDICATURE AT LAHORE. *

Before Mr. Justice Harrison and Mr. Justice Dalip Singh.

[23rd February, 1928.]

N. D. Radha Kishen and Sons of Rawalpindi .. Assesseees.

v.

The Commissioner of Income-tax, Punjab and N.W. Frontier Province .. Referring Officer.

Income-tax Act (XI of 1922) Secs. 10 (2) (iv), (vi) and (vii) and 66 (2) and (3)—Machinery and plant not used in business in account year—Depreciation and obsolescence claims, if allowable—"Used for the purposes of the business", meaning of—Reference to High Court on specified points—Assessee's right to raise other points not referred—Jurisdiction of the High Court.

The expression "used for the purposes of the business" in Sec. 10 (2) (iv) means used for such purposes during the accounting year and consequently the allowance for depreciation under Sec. 10 (2) (vi) is inadmissible in respect of buildings, machinery, plant etc., remaining idle and not actually used by the assessee in his business during the account year.

Likewise the obsolescence allowance under Sec. 10 (2) (vii) can be claimed only in respect of machinery or plant actually discarded in the accounting year.

Where on an application under Sec. 66 (2) of the Act asking for a reference on five specified points, the Commissioner stated a case in respect of two points and declined to refer the other points.

Held, that in the absence of an application under Sec. 66 (3) within the prescribed time, the assessee was not entitled in the case stated by the Commissioner to raise the disallowed points.

Case [Case No. 17 of 1927] stated under section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Punjab and N. W. Frontier Province, for the opinion of the High Court.

CASE.

In an application dated the 20th May 1926 I was asked by the petitioners to review their assessment for 1925-26 under section 33 and, alternatively, to refer a number of points to the High Court. By my order dated the 28th October 1926 assessable income was reduced from Rs. 23,824 to Rs. 21,145. The petitioners were then asked whether they wished any point referred to the High Court. They replied asking me to refer 5 points, which are specified in my order of the 22nd December. Three of these points I declined to

refer for reasons given in that order. The remaining two each involve a question of law which the petitioners agree should be referred in the following terms:—

(a) Do the words “used for the purposes of the business”, which occur in section 10 (2) (iv) of the Income-tax Act and admittedly govern section 10 (2) (vi), mean that an allowance for depreciation is inadmissible in respect of buildings, machinery, plant, or furniture not actually used by the assessee in his business during the accounting year in question?

(b) Is an allowance admissible under section 10 (2) (vii) of the Income-tax Act in respect of machinery or plant which owing to its having become obsolete is discarded before the beginning of the accounting year in question?

2. The first question arises out of the fact that in 1920 the petitioners, who have a motor-car agency at Rawalpindi, bought a Thornycroft car for the purposes of their business but never used it in their business, as they found it was too costly to run at a profit. In connection with the assessment for 1925-26, a claim for depreciation on the car was rejected on the ground that the car was not used in the business in 1924-25, the accounting year in question. A similar claim for depreciation in regard to machinery was rejected on the ground that, though previously used in the petitioners' business, it was not so used in 1924-25.

3. These facts are not in dispute. It is admitted that the machinery was not used in the accounting year and that the car, though bought for the business, was never used in it. It is further admitted that the words “such buildings, machinery, plant or furniture” used in clause (vi) of section 10 (2) are buildings, machinery, plant or furniture referred to in clause (iv), and that the words “used for the purposes of the business” used in clause (iv) govern the buildings, machinery, plant or furniture referred to in both clauses. But it is claimed that, as it is not expressly stated that they must be used in any particular year, depreciation is admissible irrespective of whether they were used in the accounting year or not.

4. In this view I do not agree. Section 10, to which both these clauses belong, is governed by section 3, a charging section which states that the assessment to be made each year “shall be charged in respect of all income, profits and gains of the previous year”. Sub-section (1) of section 10 states that income-tax “shall be payable by an assessee....in respect of the profits or gains of any business carried on by him”, and sub-section (2) adds that “such profits or gains shall be computed after making” certain allowances which are specified. As the profits or gains to be taxed are those of the previous year, it follows automatically that the allowance to be set off against those profits or gains must also relate to that year. Any other view would be opposed to the ordinary principles of accountancy which require that expenditure incurred in one year shall not be set off against the profits or gains of another year. This, no doubt, explains why in none of the 9 sub-clauses of the sub-section is it stated that the allowance in question is only admissible if the expenditure has been incurred in the previous year. And this limit of time must, I think, apply throughout the section wherever the question of time arises. Had a wider limit been intended, it would presumably have been specified. If this view is correct it follows that the words “used for the purpose of the business” mean that the buildings, machinery, etc., must have been used for the purposes of the business

in the previous year. I would, therefore, answer the first question in the affirmative.

5. The second question is analogous to the first. Three Overland cars, which had been used by the petitioners as taxis, were admittedly discarded before 1924-25 (the accounting year) on the ground that they were obsolete. Though discarded, they have not actually been sold. In 1924-25 they were put up to auction but no bid was received for them, and they are said to be still lying idle on the petitioners' premises. The question is whether in the circumstances an allowance is admissible under clause (vii) of section 10 (2) in the assessment for 1925-26 which is based upon the accounting year 1924-25. Clause (vii) states that an allowance may be given "in respect of any machinery or plant which in consequence of its having become obsolete, has been sold or discarded". As in the first case, it is claimed that as no specific period is mentioned, the allowance is admissible at any time after the cars have been discarded, irrespective of when this occurred. For the reasons given in discussing the first question, I consider that this view is wrong and recommend that the question, as it stands, should be answered in the negative.

6. A ruling in these terms will not prevent the claim for obsolescence being admitted when the cars are finally sold, for when this occurs the petitioners will be entitled, under clause (vi) of section 10 (2), in the assessment made on the income of the year in which they are sold, to the balance of depreciation (i.e., the difference between the original cost and the total depreciation allowed up-to-date) less the sum for which they are sold, however small this may be. So far, therefore, as the present claim relates to discarded plant, it is belated, and so far as it relates to plant that may hereafter be sold, it is premature.

Des Raj Sawhney, for the Assesseees.

Lala Jaggan Nath Aggarwal, for the Crown.

JUDGMENT.

A reference has been made by the Income-tax Commissioner in the following terms:—

(a) Do the words "used for the purposes of the business", which occur in section 10 (2) (iv) of the Income-tax Act and admittedly govern section 10 (2) (vi), mean that an allowance for depreciation is inadmissible in respect of buildings, machinery, plant or furniture not actually used by the assessee in his business during the accounting year in question?

(b) Is an allowance admissible under section 10 (2) (vii) of the Income-tax Act in respect of machinery or plant, which owing to its having become obsolete is discarded before the beginning of the accounting year in question?

The reference was agreed to by the petitioners. The view taken by the learned Commissioner is that the words "used for the purposes of the business" mean that buildings, machinery, etc., must have been used for the purposes of the business in the accounting year. He points out that this follows from the cardinal principle underlying whole of this Act. The tax is imposed on the profits or gains of the previous year, and it follows naturally and logically that any deduction claimed must also be on account of that same

period of time. In section 10, which deals with this matter, there is no distinct reference to the period, but where an allowance has to be made which covers a longer period, or which may only be ascertainable in a later year, a definite proviso is inserted to meet the case. The machinery in question regarding which a deduction was claimed was not used for the purposes of the business during the year in question. Counsel contends that though not used the machinery depreciated from lying idle. Whether it did so or not it appears to us that the allowance is granted not for depreciation as such but for depreciation as a consequence of the earning of income or while employed in the earning of income. Once it is conceded that the machinery in question lay idle, there is no question of such earnings. The answer, therefore, to the first question is that the words "used for the purposes of the business" mean used for such purposes during the accounting year.

As regards the second question, we are only concerned with the actual reference made, and we have no hesitation in holding for the same reason as we have given in deciding the previous question, that the claim on account of discarded machinery can only be made regarding machinery actually discarded in the accounting year.

When applying to the Commissioner for a reference under section 66 (2) the petitioners claimed the reference to three other questions, all of which the Commissioner declined to refer and gave his reasons at length for doing so. The time limit prescribed for action under section 66 (3) has expired, and counsel contends that because there has been a statement of a case referring the other two points, this opens the door to the discussion of the remaining three and entitles him to ask for a decision thereon. He contends that there is no such thing as partial statement of a case and that any points alleged by him to arise in his application to the Commissioner are automatically before us in virtue of the Commissioner having referred one or more of such points. We are wholly unable to agree with this contention. In our opinion we are seized with such questions and such questions only as are raised by the Commissioner, and if the petitioners were not satisfied with his reference, it was open to them to apply within the prescribed time under section 66 (3). This they have not done and have lost their remedy, and we decline to go into any of the remaining questions raised in the application.

We answer accordingly. No order as to costs as a deposit of Rs. 100 has been made and has not been refunded.

[240] IN THE HIGH COURT OF JUDICATURE AT BOMBAY.

Before Sir Amberson Marten, Kt., Chief Justice and Mr. Justice Blackwell.

[23rd February, 1928.]

Bai Dhanbai Dadabhai Kanga

.. Assessee.

v.

The Commissioner of Income-tax, Bombay

.. Referring Officer.

Income-tax Act (XI of 1922), Sec. 50—Assessee's accounts made up according to financial year—Refund application in respect of dividends—Computation of the period of limitation therefor—"Year" in Sec. 50, if means 'calendar' year, or 'financial' year.

Where an assessment for the year 1926-27 was made on the income of the assessee's "previous year", the financial year ending with the 31st March, 1926, the period of "one year" prescribed in Sec. 50 of the Act ought to be computed from the 1st April 1926 and consequently a refund application made on the 22nd March 1927 in respect of dividend in a limited company payable to the assessee on the 21st October 1925 was within time.

Case [Civil Reference No. 23 of 1927] stated under section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bombay for the opinion of the High Court.

CASE.

Under section 66 (1) of the Income-tax Act, 1922, (hereinafter referred to as the Act), I have the honour to submit *meo motu* for favour of your Lordships' decision, the question of law set out in para 3 below relating to the interpretation of section 50 of the Act which has arisen in connection with certain proceedings for granting refund of income-tax before the Income-tax Officer, E-Ward, Bombay City.

2. *Facts of the Case.*—These are very simple. The above-named Dhanhai Dadabhai Kanga of Bhikoo Mansion 623 Parsi Colony, Dadar, Bombay, applied to the Income-tax Officer, E-Ward, Bombay, for refund under section 48 (1) of the Act on 22—3—1927 in respect of a dividend declared on 20—10—1925. While this case was pending the Income-tax Officer received another application on 7—9—1927 for refund under section 48 (3) of the Act on account of tax deducted at source on 29—1—1926 on interest on securities from one Mr. J. P. Dastoor of No. 1, Nesbit Road, Mazagaon, Bombay. In the case of *Amratlal M. Gandhi v. Commissioner of Income-tax, Bombay* (1) which I had referred to your Lordships in 1924 it was decided on 14—4—1925 that in the case of a dividend, tax was to be taken as recovered on the day it was declared. Now if we interpreted the word 'year' in the phrase "from the last day of the year in which the tax was recovered" in section 50 of the Act as meaning a *calendar year* beginning from 1st January, an application for refund on account of a dividend declared in October 1925 should have been made by 31st December 1926 at the latest because the calendar year in which the dividend was declared ended on 31st December 1925 and a year from the end of that year would bring us to 31st December 1926. Hence the application made on 22—3—1927 for refund on the above dividend would be time-barred. If, however, we took this word 'year' to mean the financial year commencing from 1st April, the dividend declared in October 1925 would fall in the financial year from 1—4—1925 to 31—3—1926 and one year from the end of that year would mean 31—3—1927. Hence the claim put in on 22nd March 1927 would be in time. In the second case, however, where interest on securities was paid on 29th January 1926 after deduction of tax at source that day, if we took 'year' to mean the calendar year beginning from 1st January, one year after the expiry of the calendar year 1926 in which the interest was drawn would bring us down to 31—12—1927. Hence the claim made in September 1927 for refund of tax deducted while paying this interest would be in time. If, however, we took the word 'year'

to mean a financial year, the interest paid in January 1926 would fall in the financial year 1—4—1925 to 31—3—1926 and a year after its expiry would give time up to 31—3—1927 only. Hence the application made for refund in September 1927 would be time-barred. Hence taking the word 'year' to mean a calendar year, case No. (1) would become time-barred and case No. (2) would be in time. If we took it to mean a financial year, case No. (2) would be time-barred and case No. (1) in time. The meaning of this word 'year' being not clear from the Act, the Income-tax Officer referred the matter to me and as this word is not defined in the Act and as the settlement of a large number of cases of refunds depends on the decision of this question, I have thought it better to get your Lordships' esteemed opinion in the matter under the powers vested in me in section 66 (1) of the Act. As regards these refund cases, the amount of refund involved in each case is generally very small but their number is large. As by far the largest number of refundees is from the poorest classes not liable to tax at all, any one of them would hardly ever think of paying a fee of Rs. 100 and calling for a reference to the High Court under section 66 (2) of the Act. Hence, for the sake of justice, I have thought it a fit case to take action *meo motu* under section 66 (1) of the Act.

3. *Question for decision of the High Court*:—The question of law for the decision of your Lordships is as under:—

Whether the word 'year' in the phrase "from the last day of the year in which the tax was recovered" in section 50 of the Income-tax Act, 1922, means a financial year beginning with 1st April or a calendar year beginning with 1st January.

4. *Opinion of the Commissioner*:—As section 66 (1) of the Act requires me to give my opinion while forwarding the reference to your Lordships, I beg to state as under:—

5. The question for decision is as regards the interpretation of section 50 of the Act which is as under:—

<p>"50. No claim to any refund of income-tax under this Chapter shall be allowed, unless it is made within one year from the last day of the year in which the tax was recovered."</p>	<p>Limitation of claims for refund.</p>
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We want the meaning of the word 'year' in the phrase underlined above. The word 'year' repeatedly occurs in the various sections of the Act but has not been defined in it. Turning therefore to the General Clauses Act, (X of 1897, India), its section 3 (59) runs as under:—

"3. In this Act, and in all Acts of the Governor General in Council and Regulations made after the commencement of this Act, unless there is anything repugnant in the subject or context,

(59) 'year' shall mean a year reckoned according to the British calendar."

The Indian Income-tax Act, 1922, is an Act of the Governor General in Council. Hence the above definition of the word 'year' applies to it *unless there is anything repugnant in the subject or context*. We will have to see therefore whether there is anything repugnant in the subject or context as far as section 50 of the Act is concerned and if there be nothing repugnant to the subject or context, the word 'year' therein must mean a year reckoned according to the

British calendar, i.e., a year commencing from 1st January and containing 365 or 366 days as the case may be according to the above calendar.

6. A consideration of the "subject or context" means our having an eye on the whole of the Income-tax Act with particular reference to its Chapter VII wherein this section 50 occurs and which applies to refunds.

7. Before tax can be refunded, it must be recovered by or on behalf of Government and there are two methods of doing this viz., (1) by direct assessment under section 23 or 44 (B) (2) and (2) by deduction at source under section 18 (2) and (3). Before, however, either assessment or deduction of tax can be enforced, the rate or rates at which it is to be levied must be laid down by the Legislature as required by the charging section 3 of the Act. These rates are prescribed for a year only and until they are laid down for a particular year, all the provisions of the Income-tax Act remain ineffective for it. They are laid down each year by the Finance Act pertaining to it which remains in force for one year only commencing from 1st April and ending on the following 31st March. Thus for the current financial year 1927-28 (1-4-1927 to 31-3-1928), the Finance Act, 1927, enacts as under:—

"Income-tax for the year beginning on the 1st day of April 1927 shall be charged at the rates specified in Part I of the 3rd schedule" (Section 7 (1), Indian Finance Act, V of 1927, India).

This is the way the Finance Act runs every year. Thus assessment of tax and deduction of tax for the purpose of recovery commence each year from 1st April and end on the following 31st March with the expiry of the Finance Act which prescribed the rate or rates of tax for that particular year.

8. As what we have to refund is tax that has been recovered for a financial year either by assessment or deduction at source, the context, taking the Act as a whole, would appear to suggest that the words "year in which the tax was recovered" in section 50 should refer to a financial year.

9. The word 'year' first appears in the Act in the charging section 3 in the phrase "where any Act of the Indian Legislature enacts that income-tax shall be charged for any year at any rate or rates applicable to the total income of an assessee, tax at the rate or those rates shall be charged for *that year* in accordance with and subject to the provisions of this Act....." It undoubtedly means there the financial year commencing from 1st April as the Finance Act which lays down the rates of tax, prescribes them for the year commencing 1st April. In section 34 too, the word 'year' in the phrase 'escaped assessment in any year' means nothing but the financial year for this very reason. Leaving aside other sections wherein the word 'year' occurs, we will now turn to section 50 itself and examine further closely the "subject and context" to see whether 'year' therein means a 'financial year' or a 'calendar year.'

10. This section 50 applies to claims to refunds under sections 48 and 49 of the Act. Section 48 (1) deals with refunds on account of dividends, section 48 (2) deals with refunds to partners of registered firms and section 48 (3) deals with refunds of tax deducted at source on salaries and interest on securities. Section 49 deals with refunds of double income-tax charged here as well as in the United Kingdom. Taking up first 'dividends,' recovery of tax thereon commences on 1st April each year with the passing of the Finance

Act, and all refunds thereon pertain to this recovery in a financial year. Turning to registered firms, here too recovery of tax is always for a financial year for which alone their assessments are fixed and interpreting the word 'year' in section 50 as meaning a 'calendar year' will actually lead to an absurdity as under:—

Take the case of such a firm paying tax for the past financial year 1926-27 in February last and for the current year 1927-28 in November next. This is what very frequently happens and is not at all an exceptional case. If we interpret the disputed word 'year' in section 50 to mean a 'calendar year,' the time limit for applications for refunds for the year 1926-27 will extend to 31—12—1928 as tax was recovered in the calendar year 1927 and a year after its expiry means 31—12—28. Tax for the current year 1927-28 to be recovered in November 1927 will also fall in the calendar year 1927 and hence the period of applications for refunds for it too will be upto 31—12—1928 and no further. Thus the period for applications for refund for two successive financial years will be the same. This seems *prima facie* absurd as the Legislature could never have meant to lay down the same time limit with regard to refund of tax for two successive years. If we take year to mean a financial year, no such anomaly arises as the time limit for refund for 1926-27 will be up to 31—3—1928 and for 1927-28 upto 31—3—1929. This is exactly what it should be.

11. Next turning to section 48 (3), it is to be noted that the present Income-tax Act itself came into force from 1-4-1922 (section 1 (3) of the Act). The Finance Act which prescribes the rates at which tax is to be levied also comes into force from 1st April each year. Hence the authority to deduct tax at source at the rates laid down begins in all cases from 1st April each year and ends with the 31st March following upto which date alone is a particular Finance Act in force. Deduction of tax at source on salaries and interest on securities begins from 1st April thus and the year of recovery of tax in the case of these sources of income also commences from 1st April each year. In their case too, if we interpret the word 'year' in section 50 as meaning a 'calendar year,' it will again lead to anomalous results. To begin with, let us take the case of a recipient of salary applying for refund of tax over-paid in the first year in which the Act came into force *viz.*, 1922-23. Suppose, he applied for refund in January 1924. Tax began to be recovered from April 1922. Hence, if 'year' in section 50 is interpreted as meaning a 'calendar year,' the claim for tax recovered from 1st April 1922 to 31st December 1922 will be time-barred and that for tax from January to March 1923 will be in time. Thus a refund claim for a year will be partly in time and partly time-barred, a result which does not appear to have been contemplated at all by the Act as can be seen from its section 18 (5) which distinctly lays down that credit for the tax deducted at source on salaries must be given "in the assessment made in the following year." The following year in this case would be 1923-24. Hence credit must be given till that date for tax deducted at source and to decline to give a refund for April to December 1922 would be tantamount to decline to give credit as required by this section. Exactly the same would be the case as regards tax deducted in any other financial year. This result would, however, never follow if we interpreted the word 'year' to mean a 'financial year.' In that case, the above refund claim would be in time upto 3—3—1924, *i.e.*, upto

the time an assessment could be made in the year following the year in which the tax was deducted.

12. Taking up section 49, if 'year' is taken to mean a calendar year, the anomaly in the case of registered firms referred to above will arise here too. Whenever a firm pays tax for two successive financial years in one calendar year, the time limit for refund applications will be the same for both of them.

13. From the above, it appears to me that interpreting the word 'year' in the phrase 'year in which the tax was recovered' in section 50 as meaning a calendar year would be repugnant to the subject and the context leading to anomalous results which *prima facie* could not have been contemplated by the framers of the Act, the whole structure of which is based on the financial year, its very existence being for that year alone. In all cases of doubt, fiscal statutes are to be interpreted in favour of the subject and from that point of view too, we should take the word to mean a 'financial year', as interpreting it to mean a 'calendar year' will virtually cut down the period of applications for refund to 9 months only instead of 12 in most cases, as no application for a refund can be made till the expiry of the financial year when alone the total income which will determine the rate of refund, can be calculated. Hence for tax paid between April to December of a year the time to apply for refund will commence from the following 1st April and will end on the following 31st December giving 9 months instead of 12 as contemplated by the Act. Thus on account of tax on salary received from 1st April to 31st December 1926, an application for refund can only be made on or after 1—4—1927 when the total income for 1926-27 which will determine the rate of refund will be known and the time for application for refund will be upto 31—12—1927 only for tax recovered from April to December 1926. Hence the refundee will have 9 months only to apply for refund for tax deducted from April to December 1926. If the word is interpreted as meaning a financial year, there will be full 12 months to apply for refund of this tax. Of course, as regards tax deducted from January to March 1927 in the above example, the tax-payer will have time to apply for a refund from 1—4—1927 to 31—12—1928, i.e., 21 months in all. Hence in exceptional cases in which a man has had salary income from January to March only or income from dividends declared in these months only, there will be more time to apply for refund under the 'calendar year' view. However, as the number of such exceptional cases is comparatively small, on the whole the 'financial year' view will be more favourable to the subject.

14. For the above reasons, I am respectfully inclined to interpret the word 'year' in the phrase 'from the last day of the year in which the tax was recovered' in section 50 as meaning a financial year.

15. A copy of your Lordships' decision in the matter may kindly be certified to me as required by section 66 (5) of the Act for further action. The favour of a very early decision is requested as settlement of a large number of refund applications depends on it.

The Advocate-General with the Government Solicitor, for the Crown.

The Assessee not represented.

JUDGMENT.

MARTEN C. J.—This income-tax reference depends primarily on the construction to be given to section 50 of the Income-tax Act which runs: "No

claim to any refund of income-tax under this Chapter shall be allowed, unless it is made within one year from the last day of the year in which the tax was recovered."

The question before us is whether the expression "one year" and "the year" there means a calendar year or a financial year or otherwise. I say "or otherwise" because under section 2 (11) of the Act, the expression "previous year" is given a particular statutory meaning which, shortly speaking, enables the assessee to put forward his accounts either for the financial year beginning on the 1st April, or for the actual year for which he ordinarily makes up his accounts. That is because the charge of income-tax under section 3 of the Act is really in the nature of a charge on notional income *viz.*, not the actual income of the year of assessment but the income of the previous year calculated in accordance with section 2 (11) of the Act.

However in the present case we are not concerned with this last point, because the assessee did not make up her accounts differently from the ordinary financial year. Her return, for instance, for the year 1926-27 is based on her income for the financial year ending 31st March 1926. Unfortunately the claim involved here is trifling—a matter of Rs. 5—in respect of a dividend in a limited liability company which was declared at a general meeting on the 8th October 1925 and was payable from the 21st October 1925. Her application was made on the 22nd March 1927. If then for the purposes of section 50, we take the year to be the financial year, then she is within time. On the other hand if the calendar year is taken, she is out of time.

I also regret the small amount involved here, because it results in there being no appearance for the respondent, and consequently we have not got the benefit of any argument on her behalf. But as we propose to decide the particular question submitted to us in her favour and as the argument presented to us by the learned Advocate General is to the same effect, it seems to us unnecessary, having regard to the fact that we have only heard this appeal *ex parte*, to deal at any length with the Income-tax Act, or indeed to regard our present decision as necessarily binding in any other case, where we may have the advantage of arguments on both sides.

It will, therefore, be clearly understood that in the present case we are only dealing with an applicant who makes up her accounts in accordance with the ordinary financial year and not otherwise. That being so, it seems to me to be clear that the whole scheme of the Act is that there should be a financial year beginning on the 1st April of each year, and that the charge for the tax should be in respect of that particular year. This is borne out by the Finance Act (No. XIII) of 1925 which provides for the income-tax "for the year beginning on the 1st April 1925." It also receives some support from the General Clauses Act, S. 3 (19) which provides that the financial year means the year commencing on the 1st day of April. On the other hand the word "year" in sub-section 59 is defined to mean a year reckoned according to the British calendar, unless there is anything repugnant in the subject or context.

We have been through all the relevant sections of the Income-tax Act, and it seems to us that it would be repugnant to the context to construe the expression "year" in section 50 as meaning a year reckoned according to the British calendar. I may note that section 18 provides for payment of the tax by deduction at the source and that section 18 (5) provides for credit for such

deduction being given to the assessee in the following year unless a refund has been obtained. Section 34 deals with income which escapes assessment in any particular year. Sections 48 and 49 deal with refunds. Section 59 (2) (d) contains a power to make rules for prescribing the year to be taken for the purposes of section 49, which section does not apply in the present case. But I purposely do not discuss these sections, because possibly one's observations might prove embarrassing in some subsequent case where both sides were represented by counsel.

Similarly we do not propose to answer the general question that has been submitted to us in the exact form in which it is asked. Our answer to it is that in the case of Bai Dhanbai now before us the "one year" mentioned in section 50 of the Income-tax Act ought to be calculated from the 1st April 1926, and that accordingly her application made on the 22nd March 1927 was within time. There will be no order as to costs.

BLACKWELL. J:—I agree.

[241] IN THE HIGH COURT OF JUDICATURE AT BOMBAY.

Before Sir Amberson Marten, Kt., Chief Justice and Mr. Justice Kemp.

[27th February, 1928.]

Messrs. Girdhardas Harivallabhdas

Assessees.

The Commissioner of Income-tax, Bombay

Referring Officer.

Income-tax Act (XI of 1922), Secs. 10 (2) (ix) and 24 (1)—Sale of Mills to limited company—Price paid to Vendors by allotment of shares in the company—Contract to underwrite portion of allotted shares—Underwriter borrowing from Bank for taking the shares—Vendors guaranteeing loan to underwriter—Vendors doing business as Agents of the limited Co. as well as other Mills—Recovery of loan from guarantors—Alleged loss therefrom, if claimable as a business expense of the guarantors—If capital expenditure.

One M. & Co., the owners of the Jubilee Mills, sold the Mills to a limited company, the Jubilee Mills Co., Ltd., for Rs. 50 lakhs, the price being paid by allotment of fully paid 10,000 ordinary and 5,000 preference shares of Rs. 100 each, of the total face value of Rs. 40 lakhs (being the entire capital of the Jubilee Mills Company Limited, including the assumed premium of Rs. 250 per each ordinary share) and Rs. 10 lakhs in cash. Out of the shares so issued, one S entered into an underwriting contract to take up 3,800 ordinary shares at Rs. 351-4-0 per share and in respect of 750 of these underwritten shares one L entered into something in the nature of a sub-underwriting contract. For payment of these 750 shares L borrowed from a Bank on the security of these as well as other shares and M. & Co., guaranteed to the Bank this advance to L. On L becoming insolvent the Bank recovered the advance from the guarantors, M. & Co.

The assessees, who had a 9/16 share in M. & Co., doing business as Secretaries, Treasurers and Agents of the Jubilee Mills Co., Ltd. and two other Mills, alleging that their share of the loss in respect of these transactions

amounted to Rs. 96,031 claimed to set off this amount against their income under Sec. 24 (1) of the Act.

Held, that assuming S's underwriting contract was with the Jubilee Mills Co., Ltd., the guaranteeing of the loan to L to enable him to take up the shares underwritten by S was no part of the ordinary business of M. & Co., as Secretaries and Agents of the Jubilee Mills Co., Ltd., and alternatively, if the underwriting contract was with M & Co., it would be capital expenditure, as it was incurred in order that the capital value of M & Co.'s assets, the shares in the Jubilee Mills Co., Ltd., might be maintained or even increased. In either view, the claim for deduction in respect of the alleged loss was not allowable under Sec. 10 (2) (ix) of the Act.

Case [Civil Reference No. 12 of 1927] stated under section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bombay for the opinion of the High Court.

CASE.

Under section 66 (2) of the Indian Income-tax Act, XI of 1922, India (hereinafter referred to as the Act), and at the instance of Messrs. Girdhardas Harivallabhdas of Ahmedabad (hereinafter referred to as the assessee), I have the honour to submit for favour of your Lordships' opinion, the question of law categorically set out in paragraph 9 below *re*: the interpretation of sections 10 (2) (ix) and 24 (1) of the Act, arising out of the income-tax and super-tax assessments of the assessee for the financial year 1925-26 ended on 31st March 1926.

2. *Facts of the Case*:—The assessee is a firm with three partners, *viz.*, Mr. Mangaldas Girdhardas Parekh, his brother Chamanlal and father Girdhardas. They have a 9/16 share in the firm of Messrs. Mangaldas Mehta & Co., of Bombay, doing business as Secretaries, Treasurers and Agents of the Jubilee Mills Co., Ltd., and two other cotton mills. They (the assessee) have income from money-lending, dividends, interest on securities, house-rent and share in mill-agency commission.

3. The transaction out of which this reference has arisen relates to the sale of certain shares in the Jubilee Mills Co., Ltd., referred to above. The Jubilee Mills themselves at first belonged to the above firm of Messrs. Mangaldas Mehta & Co., which in June 1920 formed a limited liability company calling it the Jubilee Mills Co., Ltd., with a capital of 10,000 ordinary shares of Rs. 100 each issued at an assumed premium of Rs. 250 each and 5,000 preference shares of Rs. 100 each. The Mills were sold by the said Messrs. Mangaldas Mehta & Co., to the above limited company for Rs. 50 lakhs which were paid by allotting to them as fully paid the above 15,000 Ordinary and Preference shares of the total face value of Rs. 40 lakhs (including the assumed premium of Rs. 250 per each Ordinary share) and ten lakhs in cash. Messrs. Mangaldas Mehta & Co., were also appointed Secretaries, Treasurers and Agents of this Company. As the old proprietors owned thus all the shares issued by the new company, they were also the new proprietors in reality.

4. As the purchase consideration consisted of Rs. 40 lakhs in shares, until these were unloaded on the public, the partners of Messrs. Mangaldas Mehta & Co., including the assessee could not get their shares in the full

amount of Rs. 50 lakhs in cash. It is alleged that when the company was floated in 1920, one Sarabhai Dahyabhai agreed to underwrite 3,800 of these Ordinary shares at Rs. 351-4-0 per share but that he paid nothing in cash. The amount due from him was debited to his account and as the shares were sold, he made payments which went to the partners of the old firm of Messrs. Mangaldas Mehta & Co., including the assesseees. They were therefore naturally anxious to get the shares sold in order to recoup in part at least the purchase consideration received in shares. By 31st December 1921, Sarabhai paid them all the money due from him for the shares taken up by him.

5. As stated above, the Mills were sold to the limited company in June 1920 and the assesseees allege that in July 1920, one Lalji Govindji agreed to purchase 750 Ordinary shares of the company through Sarabhai. He too had, however, not enough money to pay for them. The assesseees who were partners in the firm of the Managing Agents of the Industrial Bank of Western India, thereupon, got a loan advanced to him by the bank amounting to Rs. 2,43,750 on the security of the above 750 shares and 20,000 shares in the Mulji Haridas Mills Co., Ltd., (Rs. 5 paid up on each), and the verbal guarantee of Messrs. Mangaldas Mehta & Co., in which the assesseees were 9-annas partner as stated above.

6. Lalji Govindji turned insolvent thereafter and the bank could recover nothing from him. It therefore recovered the whole amount due from him including interest *viz.*, Rs. 2,45,671 from the guarantors *viz.*, Messrs. Mangaldas Mehta & Co., and handed them back the above 750 shares.

7. As the assesseees had a 9-annas share in Messrs. Mangaldas Mehta & Co., the latter firm recovered from them Rs. 1,38,231 *i.e.*, 9/16 of the amount it had to pay to the above bank and gave them 422 shares out of the 750 received from the bank. The assesseees valued these shares at Rs. 100 each (though they were supposed to be worth Rs. 350 each including the premium of Rs. 250 on each) and thus arrived at a loss of Rs. 96,031 as under:—

	Rs.
Amount paid to Messrs. Mangaldas Mehta & Co., ..	1,38,231
Less value of 422 shares at Rs. 100 each (though issued at Rs. 350 each).	42,200
	<hr/>
Balance ..	96,031
	<hr/>

8. The total income of the assesseees from all sources for the year of account which was the basis of assessment for the financial year 1925-26 was Rs. 1,56,786 and they wanted a deduction from this income of the above amount of Rs. 96,031 alleging that it was a business loss. The Income-tax Officer and the Assistant Commissioner were of opinion that the alleged loss had nothing to do with business and could not be allowed as per the decision of the Punjab High Court in the exactly parallel case of *Ishar Das Dharam Chand v. Commissioner of Income-tax, Punjab* (1). The assesseees then applied to my predecessor to revise the assessment under section 33 of the Act and grant a deduction of Rs. 96,031 and if he was unable to do so, to refer the case to the

High Court. Mr. Hartley too being of opinion that the item was not a business loss, declined to allow it and ordered the case to be referred to the High Court under section 66 (2) of the Act as requested by the assesseees.

9. *Question on which the opinion of the High Court is required:—*

The question of law on which the assesseees want the opinion of your Lordships is stated by them as under:—

“Whether the allowance of Rs. 96,031 claimed by the petitioner (i.e., the assesseees) as a loss is a loss which can be set off against the petitioner’s (i.e., the assesseees’) income, under section 24 (1), under the head ‘business.’”

10. *Opinion of the Commissioner:—*As section 66 (2) requires me to give my opinion while submitting this reference to your Lordships, I beg to add as under:—

11. The assesseees have a 9/16 share in the firm of Messrs. Mangaldas Mehta & Co., and their share in any allowable loss in that firm can be set off against their income from other sources under section 24 (1) of the Act. This is not disputed. The only question is whether the alleged loss is one allowable under the Income-tax Act. As it was the firm of Messrs. Mangaldas Mehta & Co., which sustained the alleged loss, and as the assesseees can claim (as they actually do) only their share in the loss, if any, sustained by that firm and nothing else, we will have to consider the case of that firm itself to see whether this is an item which can be allowed to be deducted from its income, if any. Its business is that of Secretaries, Treasurers and Agents of the Jubilee Mills Co., Ltd., and two other mill companies and its income consists of commission from these companies. As the amount paid to the Industrial Bank of Western India under the guarantee given by it has absolutely nothing to do with the above business, it cannot be allowed as an item of deduction under section 10 (2) which specifies the allowances to be made in computing “business” income. The only part of section 10 (2) which can have, if at all, anything to do with this question, is section 10 (2) (ix), but as the above amount is not an item of expenditure incurred solely for the purpose of earning its business income viz., commission from the above Mills, and has nothing to do with it, it cannot be allowed. The firm must have stood surety merely to oblige Lalji Govindji as it is not even alleged that it did so in return for some remuneration. The standing of surety was not in the course of its business which had nothing to do with it. The business as mill-agents did not at all require the firm to stand as surety for Lalji or any one else. It was only because the vendors of the Jubilee Mills, who were the same as the partners of this firm, were interested in the sale of shares of the Jubilee Mills Co., Ltd., that the alleged guarantee was given for the loan to induce Lalji Govindji to purchase them loaded as they were with a heavy assumed premium. The case is on all fours with the case of *Ishar Das Dharam Chand v. Commissioner of Income-tax, Punjab* (1), decided by the High Court of Punjab. In that case too, the firm concerned stood surety for another firm which turned insolvent with the result that it had to pay a sum of Rs. 25,000. It was held that as the firm stood surety in order to do its friend a kindness it could not be said that the loss was incurred in connection with its business and so was not allowable. The present case is exactly of the same nature.

12. In the petition of appeal to the Assistant Commissioner, the assesses stated as under as regards this item of Rs. 96,031:—

"(4) That the Income-tax Officer in assessing the petitioner's income has disallowed the objections to the following items:—

Rs. 96,031.—The amount of the loss on account of the liability to the Industrial Bank of Western India, Ltd., incurred by Sheth Mangaldas a partner of the petitioner.

*

*

(6) That the Income-tax Officer has erred in not setting off the item of Rs. 96,031 on the following grounds:—

(a) That the petitioner firm is carrying on banking business. That one Lalji Govindji wanted a loan but as he could not be accommodated in the firm, the firm of Messrs. Mangaldas Mehta & Co., stood as surety and in the said firm the petitioner was a partner. The petitioner firm was interested in standing as surety and further it was in the ordinary course of the business of petitioner to stand as surety. The petitioner stood as surety because it would have been able to control Lalji Govindji's business. The petitioner stood as surety for a consideration and as such this amount should be allowed."

All this is word for word incorrect. In the first place, the statement that the loss was incurred by Sheth Mangaldas a partner of the assesses is wholly wrong. Secondly, as the assesses themselves never stood surety, the statement that they did so in order to be "able to control Lalji Govindji's business," if it has any meaning at all, is wholly incorrect. The statement that "the petitioner stood as surety for a consideration" is for the same reason wholly unintelligible. It was the firm of Messrs. Mangaldas Mehta & Co., that stood surety and not the assesses by themselves.

13. In the revision petition submitted to the Commissioner under section 33, the above contentions were all given up and it was alleged that the assesses suffered this loss altogether in the course of their "business, because the guarantee extended to the Industrial Bank of Western India Ltd., by Mangaldas Mehta & Co., of which the petitioner is a partner, was given purely and essentially out of regard for the business interests of the parties concerned." What is meant by "the parties concerned" is not clear but supposing that Messrs. Mangaldas Mehta & Co., were included therein, it is not at all easy to see how the guarantee given was "purely and essentially out of regard for the business interests." What had the guarantee to do with the business of the firm as mill-agents? That business did not at all require it to stand surety for loans taken from banks by would-be buyers of shares. The loss arose out of the anxiety of the partners in the firm to protect their own capital invested in mill shares and to do this they obliged their friend Mr. Lalji Govindji by standing surety for him. The alleged loss—if loss it was—is not therefore allowable to Messrs. Mangaldas Mehta & Co. It was a capital loss, and hence the assesses can claim no share in it. Messrs. Mangaldas Mehta & Co., having no income from commission in the year which was the basis of assessment for 1925-26 were not assessed at all for that year. Hence the question of this alleged loss arose indirectly when the assesses, being its 9/16 annas partners, were assessed.

14. In para 7 above, I have shown how the loss of Rs. 96,031 has been arrived at by the assesses. They have arrived at it by taking the price of

the 422 ordinary shares returned to them at Rs. 100 each. As a matter of fact there was no loss at all but a profit in the whole transaction which really amounted to an attempt to unload on the public 750 shares (including these 422 shares) which ultimately proved abortive. For these shares, they received Rs. 2,63,437-8-0 at Rs. 351-4-0 each from Sarabhai and when they were returned, they had to pay back to the bank Rs. 2,45,671. Thus there was a clear profit of Rs. 17,766-8-0. Messrs. Mangaldas Mehta & Co., got back their 750 shares and at the same time retained this sum of Rs. 17,766-8-0 while paying back Rs. 2,45,671 only to the Bank. The assessee's share in this profit was 9/16 of this sum or Rs. 9,993-10-6.

15. The way in which the loss of Rs. 96,031 has been worked out by the assessee and the various reasons given by themselves both in the appellate and the revision petition for allowing it are such as to convince any one of the frivolous nature of the claim.

16. For the above reasons, I am clearly of opinion that the alleged loss is not allowable.

17. A copy of your Lordships' opinion may kindly be certified to me for further action as required by section 66 (5) of the Act.

Sir Chimanlal Setalwad, instructed by *Messrs. Mulla and Mulla*, for the Assessee.

V. Taraporwala, with the *Government Solicitor*, for the Crown.

JUDGMENT.

MARTEN C. J.—This is a reference under the Indian Income-tax Act and the question arises under section 24 whether the assessee as partners in the firm of Mangaldas Mehta & Co., are entitled to set-off a particular loss alleged to be of Rs. 96,031 in respect of a guarantee given by that firm of Mangaldas Mehta & Co. in respect of one Lalji Govindji. It will, therefore, be clearly understood that the firm whose business we have to consider is that of Mangaldas Mehta & Co.

Now under section 24 we have to see the various heads on which income-tax is payable. That will be found in section 6 which includes (iv) business and (vi) other sources. Then section 10 provides that the profits or gains shall be computed after making the following allowances, viz., (ix) "any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains." Therefore, we have to consider whether this alleged loss of Rs. 96,031 was incurred by Mangaldas Mehta & Co., solely for the purpose of earning profits or gains in their business, or whether it was in the nature of capital expenditure. Unfortunately the final case, as stated to us, is, I regret to say, wanting in many relevant particulars. For instance, agreements are mentioned without stating between whom they were entered into. Dates are not given, nor in some cases are the relevant figures. But doing the best one can with the materials before the Court the following appear to be the more salient points.

This firm of Mangaldas Mehta & Co., were the owners of the Jubilee Mills. In June 1920 they as vendors and promoters converted these mills into a limited liability company, and agreed to take as the purchase price 50 lakhs

of Rupees, payable as to 40 lacs in shares, and as to 10 lacs in cash. Apparently the share capital of the Company was 10,000 shares of Rs. 100 each (which were to be issued at Rs. 350), and 5,000 preference shares of Rs. 100 each. That makes at the issue price 35 lacs for the ordinary shares and 5 lacs for the preference shares. If then the whole of the share capital was to go to the vendors, it is not clear how the Company was to find the remaining 10 lacs in cash as the balance of the purchase price.

However that may be, it appears that one Sarabhai entered into an under-writing contract to take up 3,800 shares, presumably ordinary, at Rs. 351-4-0. We are not told with whom this contract was entered into, but as the shares were all to be issued to the vendors, it is difficult to see how Sarabhai could have entered into an under-writing contract with the Company in respect of these shares, and still less so when he was to underwrite them at Rs. 351-4-0, whereas they were to be issued to the vendors at Rs. 350. The probabilities are, I think, that the shares in question were really offered to the public by the vendors and that the under-writing contract was with the vendors. Consequently in the statement in the case "By 31st December 1921, Sarabhai paid them all the money due from him for the shares taken up by him," the word 'them' means the vendors and not the Company. It would seem clear that the Company having agreed to issue the shares to the vendors could not issue them to Sarabhai, unless at any rate the vendors consented.

So much for Sarabhai. But it appears that there was something in the nature of a sub-under-writing contract by one Lalji Govindji, and he is the person with whom we are mainly concerned. Unfortunately we are not told with whom Lalji Govindji entered into this sub-contract, nor are we given the exact date, but it is stated to be July 1920. The exact statement before us is:—"The assessee alleges that in July 1920 one Lalji Govindji agreed to purchase 750 ordinary shares of the Company through Sarabhai." Stopping there, I think it is the duty of the Commissioner to find the relevant facts specifically and not to deal with important statements as being mere allegations by one side or the other. Anybody can allege anything—even that black is white. But we want to know and are entitled to have definite findings of fact by the Commissioner, because we are judges here of law and not of fact.

Now it appears that these 750 shares which Lalji Govindji agreed to take up were part of Sarabhai's 3,800 shares. I am not sure that that is specifically found by the Commissioner but that is how the case was opened to us. Lalji apparently had not the money to take the shares and so he borrowed a sum of Rs. 2,43,780 from the Industrial Bank of Western India on the security of these 750 shares of the Jubilee Mills Limited and on some shares of another mill with which we are not concerned. Where Mangaldas Mehta & Co. come in is that they guaranteed to the Bank this advance to Lalji.

The next incident is—again we are not told the date—that Lalji became insolvent; and eventually the Bank recovered the amount of the advance from the guarantors, Mangaldas Mehta & Co.

The next step is that the assessee claims that their share of this loss as partners in Mangaldas Mehta & Co. amounts to the sum I have already mentioned of Rs. 96,031. There is however a dispute of fact as to that; the Commissioner says that there was no loss but there was in point of fact a profit to Mangaldas Mehta & Co. on this transaction.

Now if we had thought it necessary to send this case back to ascertain precisely for whom Sarabhai underwrote these shares, we should have done so. But it seems to us that it is unnecessary because in our view the assesses must fail whichever is the true view of the case. Supposing, which in my opinion is not the fact, that Sarabhai under-wrote by a contract with the Company, then so far as the Company was concerned it had got its full under-writing contract for these 3,800 shares. It was no concern of the Company as to whether Sarabhai did or did not get any sub-under-writing contract. The utmost that can be said and which was put to us by Sir Chimanlal is that the Company would be interested in seeing that their head under-writer got rid of his shares, because otherwise he might not be able to meet his obligations under his under-writing contract. As far however as this case is concerned there is nothing whatever to show that Sarabhai was not in a position to carry out the whole of this under-writing contract with the Company. That being so, the Company had no interest, as I have already said, in this sub-under-writing contract. One may perhaps go further and say that to relieve a contractor with the Company of his obligations in this way would really be no part of the business of the Company and still less that of its agents. Therefore in that view of the case it seems to me that this loan to Lalji Govindji in order to enable him to take up certain shares which in fact Sarabhai had under-written was no part of the ordinary business of Mangaldas Mehta & Co. as agents of the Company. It is, therefore, in no way an expenditure incurred solely for the purpose of earning such profits or gains within the meaning of section 10, sub-section (ix).

Now I will take the alternative case, *viz.*, that Sarabhai really underwrote with Mangaldas Mehta & Co., who were the vendors. Here we have a case where Mangaldas Mehta & Co. owned a particular property—the Jubilee Mills. That landed property with its chattels was to be turned partly into cash of Rs. 10 lacs and partly into shares worth 40 lacs. Therefore I can quite understand this that Mangaldas Mehta & Co. were interested in seeing that their new assets in shares appreciated in value. Therefore they might very well wish, as the Commissioner puts it, to unload the shares on the public so as to convert them into cash at the earliest possible moment. Their interest, therefore, in the under-writing contract of Sarabhai I can understand, and to a lesser degree in that of Lalji Govindji. But that had nothing to do with their business as Agents of the Company. It would be in their position as owners of a certain property. And if the result of this under-writing contract with Sarabhai or of this sub-under-writing contract with Lalji Govindji was to increase the value of the assets, I fail to see how that can be regarded as either an income profit or an income loss. To my mind that would be within the meaning of section 10 (ix) in the nature of capital expenditure, *viz.*, an expenditure incurred in order that the capital value of these assets might be maintained or even increased. That, so far as I can see, is the highest at which the assesses' case can be put, and in my opinion it fails on that point alone. Mangaldas Mehta & Co. were not carrying on a trading business in the sale and purchase of shares. And there was here no trading loss, which could properly be debited to profit and loss account.

Speaking then very generally I agree with the opinion expressed by the Commissioner that this business of guaranteeing the Bank's loans to Lalji

Govindji was really no part of the business in respect of which the assesseees have been assessed. Consequently in my judgment the assesseees are not entitled to make the deduction which they have claimed, and the question submitted to us should be answered accordingly. Under these circumstances it is unnecessary to consider the alternative case put forward on behalf of the Crown, viz., that there was no loss at all, but on the contrary a profit. The assesseees' answer is that that is only arrived at by neglecting the subsequent fall in the value of the shares. However as I have already said, I do not think it necessary for us to answer that particular question. In the result then I would answer the formal question submitted to us in paragraph 9 in the negative. The assesseees must pay the costs of the reference as on the Original Side scale.

KEMP, J.—I entirely agree with the judgment of the learned Chief Justice and would only add that with reference to the question whether there really was a loss or not, the assesseees' learned Counsel claims that the losses arose through the depreciation of the shares which were taken at Rs. 250 premium and are estimated in the assesseees' calculation at Rs. 100. With regard to this I may point out that nowhere in the case stated have we any evidence that the shares depreciated to the extent mentioned in this calculation. In the absence of such evidence it seems clear that the firm of Mangaldas Mehta & Co. received from Sarabhai the sum of Rs. 2,63,437-8-0 at a premium of Rs. 251-4-0 for the 750 shares and paid back to the Bank Rs. 2,45,671-0-0. Mangaldas Mehta & Co., therefore made a profit of Rs. 17,766-8-0 and the assesseees' share in this profit would be Rs. 9,093-16-0. I answer the question referred to us in the negative.

[242] IN THE HIGH COURT OF JUDICATURE AT BOMBAY.

Before Sir Amberson Marten, Kt., Chief Justice and Mr. Justice Kemp.

[28th February, 1928.]

The Ahmedabad New Cotton Mills Co., Ltd.

Assesseees.*

The Commissioner of Income-tax, Bombay

Referring Officer.

Income-tax Act (XI of 1922), Secs. 3 and 13—Return of income undervaluing opening and closing stock of the year—Income-tax Officer revaluing closing stock only at true value—Refusal of assessee's claim for revaluation of opening stock—Proper basis or computation of the profits of the year—Opening and closing stock to be given true value—Reference to High Court—Proper mode of submission.

The assesseees in returning their income for the year ending with 31st December, 1925 put in a profit and loss account and a balance sheet wherein their opening and closing stock for the year were written down at an undervaluation, the valuation of the opening stock at the beginning of the year corresponding with the value of the closing stock at the end of the previous year, 1924. The Income-tax Officer on enquiry found that the closing stock was grossly undervalued and valuing the same at its true value made an assessment

* (1928) I.L.R. 52 Bom. 669; 30 Bom. L.R. 1160; A.I.R. (1928) Bom. 510.

accordingly, declining to revalue the opening stock similarly. The assesseees, while admitting the undervaluation claimed that in determining the assessable profits of the year the opening stock alleged to have been likewise undervalued, should also be revalued. On a case stated by the Commissioner of Income-tax under Sec. 66 (2) of the Income-tax Act as to the correct basis for determining the assesseees' income,

Held, that for the proper computation of the profits of the year in question, the assesseees' stock both at the beginning and end of the year should be valued at its true value, as the revaluation of the closing stock alone would result in arriving at a fictitious profit and not the true profits of the year.

Chengalvaroya Chetty v. Commissioner of Income-tax, Madras, 2 I.T.C. 14, Referred to.

Observations on the proper mode of submitting References to the High Court.

Case [Civil Reference No. 15 of 1927] stated under section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bombay for the opinion of the High Court.

CASE.

Under section 66 (2) of the Income-tax Act (XI of 1922, India) (hereinafter referred to as the Act) and at the instance of the Ahmedabad New Cotton Mills Co., Ltd., of Ahmedabad (hereinafter referred to as the assesseees), I have the honour to refer to your Lordships the question of law categorically set out in para. 4 below *re* the interpretation of sections 10 and 13 of the Income-tax Act, 1922, which has arisen in the course of the assessment of the above assesseees for the year 1926-27 ended 31st March last.

2. *Facts of the Case:*—The assesseees are a limited company doing business at Ahmedabad. For the purpose of their assessment for the last financial year, *viz.*, 1926-27, they put in, as required by section 22 (1) of the Act, a return of income supported by a printed Profit and Loss Account and Balance Sheet in Gujarati (a translation of this in English submitted by the assesseees for the purposes of this reference accompanies as Exhibit A*). On enquiry, however, the Income-tax Officer found that the closing stock of cotton, yarn, cloth, cotton waste and coal was grossly undervalued so as to show less profit. Under the mercantile system of accountancy, which the assesseees professed to follow, gross profit in the trading account for a year is to be arrived at as under:—

Dr.

Cr.

Opening stock as brought forward
from the preceding year.

Sales for the year.

Purchases for the year.

Closing stock at the end of the year.

The excess or deficit of the total of the credit side over the total of the debit side is the gross profit or loss in the trading account. According to the well established and universally recognised principle of accountancy, the opening stock is merely the figure of closing stock for the previous year carried forward. The closing stock is to be valued at cost or market price which—

ever is lower at the date of the Balance sheet (*vide* please Practical Auditing by Spicer and Pegler, page 172). The actual valuation of the closing stock by the assesseees compared as under with the valuation according to the above rule :—

Stock and stores.	Valuation by the assesseees.	Valuation as per the rule of cost or market price whichever be the lower.
Cotton ..	Rs. 5-0-0 per maund.	Rs. 18-2-6 per maund.
Cloth ..	„ 0-7-0 per lb.	„ 0-11-10 per lb.
Yarn ..	„ 0-2-0 „ „	„ 0-5-0 } to } per lb. „ 1-8-0 }
Cotton waste ..	„ 1-4-0 per maund.	„ 2-0-0 per maund.
Coal ..	„ 4-6-0 per ton.	„ 10-0-0 per ton.

It is of course self-evident that the lower the valuation of the closing stock, the smaller the profit for the year. The total value of the closing stock as per the assesseees' valuation was Rs. 3,03,893-4-10 whereas according to the valuation as required by the above rule of accountancy, it came to Rs. 8,21,201-4-10, the undervaluation thus being to the extent of Rs. 5,17,308. The assesseees' valuation was thus barely 37 per cent. of the correct valuation. Its result was that profit was shown less to the extent of Rs. 5,17,308. In the case of income from business, profit is to be computed as laid down in section 13. As the assesseees' method did not disclose the true profits, the Income-tax Officer under the powers given him by section 13 to compute profits in such manner as he "may determine" in such cases, adopted in his computation of the profit liable to tax, the proper valuation as per the above rule of accountancy and added the above amount to the profit for the year. He levied accordingly income-tax and super-tax on an income of Rs. 7,66,450 though according to the valuation of the assesseees, the income was Rs. 2,49,142 only.

3. Against the above assessment, the assesseees appealed under section 30 of the Act to the Assistant Commissioner of Income-tax, Northern Division. That Officer confirmed the assessment. Before him, it was admitted that the undervaluation was to the extent stated by the Income-tax Officer, but that as the assesseees had undervalued the opening stock too similarly, it too should be revised and revalued. Other grounds too were advanced before him against the assessment but as they have nothing to do with this reference, I need not trouble your Lordships with them. The Assistant Commissioner decided the appeal against the assesseees saying that the opening stock must be taken as per the valuation made by the assesseees themselves at the end of 1924 and accepted by the Income-tax Department and on the basis of which tax was already paid for the year 1925-26. Not satisfied with this decision, the assesseees asked me either to order the Income-tax Officer to revalue the opening stock too or refer the matter to your Lordships. As I consider their request to have the opening stock revalued wholly unreasonable, I have to trouble your Lordships as required by section 66 (2) of the Act.

4. *Question for the opinion of the High Court*:—The question of law which the assesseees want to be referred is as under as stated in their petition to me:—

“When the opening and closing stocks are both undervalued whether the real profits of the company of a particular year can be ascertained by merely raising the valuation of the closing stock, not taking into consideration the similar undervaluation of the opening stock.”

The question is a bit clumsily stated but apparently the assesseees want your Lordships to state whether under the law, when an assessee is found to have grossly undervalued the closing stock, he can require the Income-tax Officer to revalue the opening stock too, alleging that it too was similarly undervalued.

5. *Opinion of the Commissioner*:—As section 66 (2) requires me to give my opinion while forwarding the reference, I beg to state as under:—

6. The question as framed by the assesseees takes it for granted that in this case the opening stock too has been grossly undervalued. No enquiry has, however, been made by the Income-tax Officer regarding the opening stock which has been and must be under the rules of accountancy and as required by common sense taken at exactly the same figure as the closing stock for the previous year. It cannot, therefore, be said whether it has or has not been also grossly undervalued as alleged. However, even taking it for granted that it is so undervalued, there is nothing in the Income-tax Act or anywhere else under which an assessee can claim to have the opening stock revalued having once valued it at a certain figure and paid tax on the basis of that valuation. In order that all profit or loss may be fully brought to account and tax paid on it, it is absolutely essential that the figure given in the trading account of a year as the value of the closing stock should be identical with the figure given in the trading account of the following year as the value of the opening stock. Else endless confusion will arise and an assessee may go on showing fictitious losses every year to the Income-tax Department and a Company might go on showing fictitious profits to its shareholders. The proposition put forward on behalf of the assesseees appears to be entirely erroneous as can be clearly seen from the following extract from the standard work on Accountancy by Mr. F. W. Pixley, F.C.A. (late President of the Institute of Chartered Accountants in England and Wales) (page 168) who states as under regarding this question:—

“As there is no interregnum in the career of a going concern, it must be considered that the Stock has been purchased at the same price as that at which the same concern took credit for it at the close of business the previous evening, upto which time the preceding Trading Account is prepared. The value therefore to be inserted as the first item on the debit side of a Trading Account is the exact figure at which the Stock-in-trade was valued the evening before”.

Thus according to this authority, the first item on the debit side of the trading account must be the *exact figure* at which the balance of stock-in-trade was valued at the end of the preceding year.

7. In *Chengalvaroya Chetty and Munisami Chetty v. Commissioner of Income-tax, Madras* (1) the Madras High Court has already decided this ques-

tion regarding the revaluation of the opening stock saying that an assessee cannot require the Income-tax Officer to take the opening stock for a year at any other figure than that for the closing stock in the previous year's Balance Sheet. In that case, the assessee valued his closing stock for the year 1921-22 at Rs. 6 per piece. The next year he wanted the same stock to be revalued as the opening stock at Rs. 13-8-0 per piece. By valuing the stock at Rs. 6 per piece at the end of 1921-22, the assessee had worked out a loss of Rs. 1,03,007 for that year. In the following year, taking the opening stock at the same figure as the closing stock for the preceding year, there was a profit of Rs. 43,740. Had he valued the closing stock for 1921-22 at Rs. 13-8-0 per piece instead of Rs. 6, the loss for that year would have been Rs. 46,209-8-0 and for 1922-23, instead of any profit, there would have been loss amounting to Rs. 13,057-8-0. He would thus have got exemption for both years. The assessment based on the income for 1921-22 would not have been in any way altered by adopting the rate of Rs. 13-8-0 for the closing stock instead of Rs. 6 as there being still loss, no tax was payable. Still, however, the Madras High Court declined to allow the question of valuation of the opening stock to be reconsidered and ordered it to be taken at the same price as that shown in the Balance Sheet for the preceding year. Chief Justice Coutts Trotter in his judgment remarked that the proposition that the opening stock for a year must be taken at the same figure as the closing stock for the preceding year "seemed so obvious that we must scrutinise carefully what" was "said against it" and added "The principle, if it can be called a principle, contended for by the assessee would enable him, having cut his loss in one year, to go on claiming to deduct the same loss year in and year out and I cannot illustrate the absurdity of that better than by the hypothetical case, that I put in the course of the argument." Not to talk of a hypothetical case, the assessee's case before your Lordships in itself will suffice to illustrate the absurdity of their proposition were it followed. Taking the closing stock for the year 1924 at the valuation then fixed by the assessee, the profit that year came to Rs. 2,58,733 on which tax has already been paid for the year 1925-26. Now if that stock be revalued and taken at say Rs. 5 lakhs more, the profits for that year would really be Rs. 7,58,733 as against Rs. 2,58,733 on which alone tax has been paid. Thus tax on a profit of 5 lakhs of rupees would be wholly avoided. This would be an excellent method of evading the tax and no trader need pay anything on account of tax if the principle be allowed. All that he need do is to take the stock at the close of a year at such a figure as to show no taxable income and in the following year to revalue the same stock as opening stock at a higher value so as to show very little income once again.

8. That the closing stock for the year 1925 has been grossly undervalued has not been denied by the assessee, nor have they anything to urge *re* the valuation as now fixed by the Income-tax Officer. To value closing stock neither at cost nor at market price but something far below either so as to show it at about one-third of its real value is showing a wholly fictitious state of affairs to the shareholders, the taxing authorities and every one else. The justification for the course adopted is stated as under by the assessee in the revision petition:—

"The reason is that for the last several years, we have been undervaluing the stock, not with the object of evading any income-tax but to safeguard against

all heavy fluctuations in the market, and have thereby a special reserve, and enabling the Company to equalise the dividends which it would otherwise be unable to do."

If the object of the assesseees was not to evade income-tax, it is not understood why they should now do so by insisting that the opening stock should also be revalued. To do so would certainly amount to not paying any tax at all as shown in the preceding para on the gross undervaluation which is alleged to have been going on all along. Again, if avoidance of tax was not the object, why did not the assesseees point out the undervaluation to the Income-tax Officer the very first time it was resorted to? In the Balance Sheets, as regards these valuations, the words "under cost" or "under market value" were used. These words might be taken to mean "slightly below cost" or "slightly under market value" but can never be interpreted to mean grossly below cost or market price or at about $1\frac{1}{3}$ of either of these values. Again as regards the question of equalisation of dividends, the Balance Sheet for 1925 shows that there is actually a "Dividend Reserve Fund" with Rs. 57,826-10-3 to its credit and Rs. 6,000 were carried to it from the profit for the year 1925. When such a fund actually existed, if what was taken to it was not deemed sufficient, more could have been carried to it each year instead of adopting this so-called method of creating a secret reserve. I need hardly add here that sums placed to Reserve cannot legitimately be deducted from taxable profits.

9. Now we will turn to the Income-tax Act itself to find out what it requires to be done in a case of this kind. What an Income-tax Officer has to tax is profit for the previous year calculated *as laid down in the Income-tax Act* and not as may have been calculated by an assessee for his own purposes. This is an admitted fact and the dispute is solely as regards the *true method of computing profits and gains* under the Act for the purposes of assessment. This being a case of income taxable under the head "Business" in section 6 of the Act, we have to turn to the provisions in the Act referring to the computation of profit from "Business." They are contained in sections 10 and 13 which expressly refer to the computation of profits and gains for the purposes of assessment in the case of a business. Reading these two sections together, it will be easily seen that gross profits and gains in the trading account are to be computed as laid down in section 13 and the allowances referred to in section 10 are then to be allowed therefrom to arrive at the taxable profits. It is with section 13 that we are mainly concerned and it needs careful consideration. It runs as under:

"13. Income, profits and gains shall be computed, for the purposes of sections 10, 11 and 12, in accordance with the method of accounting regularly employed by the assessee:

Provided that, if no method of accounting has been regularly employed, or if the method employed is such that, in the opinion of the Income-tax Officer, the income, profits and gains cannot properly be deduced therefrom, then the computation shall be made upon such basis and in such manner as the Income-tax Officer may determine."

Now the Income-tax Officer has in this case regarded the method employed by the assesseees to be such that the profits and gains to be taxed cannot properly be deduced therefrom and so has proceeded to compute them "in such

manner as he may determine" as required by the proviso to the above section. Enough has been stated in the preceding parās to show that the Income-tax Officer, was right in deciding that the assessee's method was such that profits could not be properly calculated therefrom. In fact, as the assessee themselves admit that there are "hidden profits" according to their system of accounts, the fact that it does not disclose all the profits or gains liable to tax needs no further proof. The method of accounting adopted being admittedly one which shows fictitious profits, the Income-tax Officer was quite justified in rejecting the calculations made by the assessee and ascertaining the taxable profits in such manner as he thought just and proper. In this connection your Lordships' attention is invited to the decision of the High Court of Judicature at Lahore in the case of *Gokal Chand Jagan Nath v. The Commissioner of Income-tax, Punjab and N. W. F. Province* (1). In that case, it has been definitely decided that under the above section 13 of the Act, "the Income-tax Officer is the sole arbiter on the question of the possibility of deducing the income, profits and gains of an assessee from the method of accounting employed by him." Hence it seems not even necessary to consider whether the Income-tax Officer was in this case justified in rejecting the method employed by the assessee as he is the sole arbiter on this point under the law. The method employed by the assessee in this case being so very faulty, even if the law had not given these powers to the Income-tax Officer, no one would have thought his action unreasonable. The proviso distinctly says that in such circumstances, the Income-tax Officer is to compute profits in such manner as *he* may determine. Hence neither the assessee nor any one else can compel him to determine them in any particular manner. An assessee cannot require him to recalculate the opening stock even in a case in which that may be an entirely reasonable demand as the law allows the Income-tax Officer alone to determine the method of computation in such cases. All that the Income-tax Officer has done in this case is to follow strictly the settled rules and principles of correct accountancy *viz.*, to take the opening stock exactly at the figure of closing stock at cost or market value whichever be the lower. Nothing can be fairer than this.

10. The assessee further say that if the opening stock is not revalued, the Income-tax Officer will really be taxing profits made in past years and hidden in the balances of stock, though under section 34 of the Act he has power to levy tax on account of income which escaped taxation in the preceding year only. This mode of argument is incorrect and irrelevant as in this case the Income-tax Officer has not taken action under section 34 with a view to tax profit made in some past years on the ground that it had escaped taxation. The case has not been dealt with under section 34 which has nothing to do with it and it is no use dragging it in. The Income-tax Officer having found the method of accounting employed by the assessee to be such that it did not disclose the true profits, has taken action under the proviso to section 13 and it is submitted that this proviso has been correctly applied. There are, I need hardly say, various methods of evading tax by not showing the true income to the authorities and in order to defeat them as far as possible and levy tax on all the profits made by an assessee, various provisions in the Act have been put in. Section 34 contains some of them and section 13 others. There are other sections too in the Act besides these which, however, need not be referred to specifically here.

(1) 2 I.T.C. 180.

Some methods of evasion can be duly dealt with under section 34, some under section 13 and some under other sections in the Act meant for them. To argue that in a case which falls under section 13 but does not fall under section 34, the evasion is permissible because both the sections do not apply to it is wholly illogical for the simple reason that the law does not require that a particular case of evasion should fall at the same time under all the sections in the Act referring to evasions including both sections 13 and 34. Section 13 and 13 alone is clearly meant for cases of this kind where accounts are so made up as not to disclose the true profits and we have to look to it alone.

11. If what the assessee alleges *re*: this creation of secret reserve is correct, surely in the past in some one year at least they must have had a bad time and in order to be able to give a dividend to the shareholders, the closing stock for the year must have been written up. When they did so, did they revalue the opening stock or did they ask the income-tax Officer to revalue it? They never did any such thing and had not this case arisen, they would never have done so in future too for the simple reason that the opening stock must invariably be taken at the price at which it has been valued at the close of the preceding year as stated above.

12. For all the above reasons, I am of opinion that the assessment levied by the Income-tax Officer is correct and that the answer to the question put by the assessee is that in arriving at the correct figure of profit liable to tax, the valuation of the opening stock must be taken at exactly the same figure as that for the closing stock for the preceding year.

13. A copy of your Lordships' opinion may kindly be certified to me for further action as required by section 66 (5) of the Act.

Sir Chimanlal Setalwad with Messrs. Mulla and Mulla, for the Assessee.

Taraporewala, with the Government Solicitor, for the Crown.

JUDGMENT.

MARTEN C. J.:—In this income-tax reference, the question in dispute is how in the assessment annexure E of the 21st September 1926 ought the Companies' stock to be valued. Ought it to be valued by valuing at its true figure the Company's stock both at the beginning and at the end of the year in question, or ought only the value of the stock at the end of the year to be taken at its correct figure.

The assessment is for the year 1926-27 and is in respect of the profits for the year 1925-26. This is under section 3 of the Indian Income-tax Act 1922 which imposes a tax in respect of profits of the previous year. Then if one turns to the definition of "previous year" in section 2 (11), one finds it means "the twelve months ending on the 31st day of March next preceding the year for which the assessment is to be made," unless as in the present case the assessee usually makes up his accounts for a different year. We are told that the assessee makes up his accounts for each year ending the 31st December. Consequently the actual year we have to take here is the year ending the 31st December 1925.

Similarly, in addition to the income-tax there is an assessment for super-tax which under section 55 is levied for the same year. The assessment here is annexure E 1, and precisely the same point arises as regards that.

Now what is common ground is that at any rate the stock at the end of the year 1925 was under-valued in the Company's return. The Company says it was also under-valued at the beginning of the year. That has not been strictly proved, but the whole case depends upon it, and therefore for the purposes of the present case we propose to assume that this is the case. Now what the Commissioner has done is this. He has rectified the value of the stock at the end of the year by substituting the true value of the stock as at that date, but he has declined to make the corresponding alteration as regards the stock at the opening of the year. He says that that ought not to be done because under a well-known principle of accountancy the opening value must be taken at precisely the same figure as the closing value for the previous year, *viz.*, the 31st December 1924, and that if anything to the contrary is done you would get into great difficulties, and would also open the door to frauds on the public revenue.

We have not got definite evidence before us as to the previous balance sheets of the Company, nor their assessment, nor as to the mode of valuation in each previous year. We are consequently unable to say on the materials before us whether it is the fact that in all previous years the stock was regularly under-valued, or whether it was not. Counsel for the Company has told us on instructions that in fact this has been the regular practice of the Company for the last 10 years, and that it has been done not with any improper motive, but in order to provide something in the nature of a secret reserve. Writing down the stock, we all know, may be a method of obtaining a reserve fund. One is familiar with it, for instance, in the case of certain shipping companies who in good days used to write down the value of their ships to a mere trifling amount per ton. But we are not actually concerned in the present case to decide that point, because as I have said the evidence is not before us. Nor can we test counsel's statement that in 1918 the income-tax authorities objected to what the Company had done, and in that year took a revised valuation both at the beginning and at the end of the year, but that subsequently the old practice was continued.

Nor are we in a position to decide the point that during the past 10 years or so this under-valuation has been known to the Commissioner. All that we have before us is his statement in para 8 "in the Balance Sheets, as regards these valuations the words "under cost" or "under market value" were "used." One may take it, therefore, that certainly the past balance sheets were before the Commissioner, and that presumably before making the various assessments the balance sheets were also before the Income-tax Officer for the several years in question. If that was so, it would appear that to some degree at any rate it was known that the stock was being taken at under cost.

Counsel, however, for the Crown says that this is a well-known expression in accountancy. It only means a reasonable margin of say 5 or 10 per cent in order to provide against risks, because after all an exact valuation of goods is not always an easy task. Some margin may fairly be allowed. But he contends that an expression like that would never cover a gross under-valuation as in the present case, for the erroneous valuation of the closing stock for the year 1925, is found by the Commissioner to be nearly 37 per cent of the correct valuation.

On the other hand counsel for the Company tendered before us a statement showing that over the past 10 years there has really been no loss of tax

to the Crown, but that taking one year with another, there has, if anything, been a loss to the Company by adopting the methods that they have. For that purpose he tendered a statement showing the past value of the stock, and—so we understood—what would be the case if the true figures had been inserted. However, the statement was objected to by counsel for the Crown, and as it had not been laid before the Commissioner and undoubtedly required verification as regards the figures for the past years, we allowed the objection, and rejected the statement and did not look at it.

On the whole however we have not thought it necessary to send the case back for further evidence under section 66 of the Act, though we have thought it proper to direct that the original assessment, which I have already alluded to of the 21st September 1926 and also the supplementary assessment of the 17th December 1926 should be treated as annexures to the reference. So also as regards the notice of the Income-tax Commissioner under section 34 of the Act, of the 2nd November 1926 and the reply of the Company of December 1926.

Now those last two documents bring me to a technical point that was raised in the case, and it is this. The supplemental assessment by the Income-tax Officer of the 17th December 1926 was made under section 23 (3) of the Act, read with section 34. There was an appeal to the Commissioner, and he at para 10 of his reference states: "The case has not been dealt with under section 34 which has nothing to do with it and it is no use dragging it in. The Income-tax Officer having found the method of accounting employed by the assessee to be such that it did not disclose the true profits, has taken action under the proviso to section 13 and it is submitted that this proviso has been correctly applied."

It is now admitted that in this respect the Commissioner was inaccurate. The proper section to apply here was section 34. It was under this section that the assessment before him was actually made, and it was not open to the Commissioner to ignore the section and yet to treat the previous assessment as wrong. Further, as regards section 13 there is no provision for a notice under section 13. Other sections deal with notices. Section 13 merely deals with the manner in which a particular assessment is to be arrived at so far as regards the method of accounting to be adopted.

That being so, an argument was submitted to us by the Company that it was necessary for the Income-tax Officer to issue, in addition to a notice under section 34, a notice under section 23 (2), if the officer had reason to believe that the supplemental return made in pursuance of the notice under section 34 was incorrect. However, this was merely a technical point. One answer made to it was that under section 34, the provisions of the Act were only to apply "so far as may be" to a notice issued under section 34, and that accordingly a further notice under section 23 (2) was unnecessary. However, eventually it became unnecessary for us to decide this point because counsel for the Company was willing to waive it, and to treat the case as if any notice necessary under section 23 (2) had in fact been given.

I can therefore now deal with the point we have really got to decide, and in my judgment that point depends on section 3, *viz.*, the charging section. What then was the income of this Company for the previous year, *viz.*, the year ending the 31st December 1925. Supposing for the sake of argument the

Company had only started business in that year, it would to my mind be clear that whatever the Company's return had said, the proper mode of ascertaining the profits would be to take at its correct figure the value of the stock both at the beginning and the end of the year. It would be wrong to adopt the method of accepting the Company's return for the beginning of the year and only to rectify the figures at the end of the year. But it is argued that the Commissioner is entitled to do that in the present case, and thereby in effect to put an under-value on the stock at the beginning of the year, because that under-value existed at the close of the preceding year as the Company had been trading in the previous year.

Then the argument runs that under the rigid rules of accountancy it follows that whether the closing figure of the year before was right or wrong, it must be adopted at the beginning of the year 1925. But to my mind there is a fallacy in adopting that as an universal rule incapable of any alteration. I quite appreciate that in an ordinary way that may be the proper course to adopt in arriving at the profits, although in *Chengalvaraya Chetty v. Commissioner of Income-tax, Madras* (1) it is described as a rough and ready manner of ascertaining the profits. But if, for instance, a mistake or an error has been made in the previous year as regards the stock in question surely there must be some way of correcting it in the subsequent year. If for instance, for any particular year a Company has to show a true profit and loss account, or a true balance sheet, you don't necessarily arrive at a true result by accepting the valuation of the previous year. You may still get a fictitious profit for the particular year you are dealing with.

So, here, it seems to me that the method which the Commissioner proposes will result in a fictitious profit. It will not be a true profit for the particular year in question, *viz.*, the year ending 31st December 1925 but will be something entirely different. The Commissioner's proposal may in this particular case benefit the Crown. In other cases it might not, but with that we are not concerned. The true principle to my mind is that under the Act you must ascertain the true profits for a particular year.

But I wish to guard myself very clearly against it being thought that we are in any way laying down any proposition, which will enable people to play fast and loose with their closing and their opening valuations. We are doing nothing of the sort, and nothing that I have said is to be taken to lead any one to believe that it is open to an assessee to adopt any arbitrary method of valuation he may like, and still less that he may take any course which will tend to defraud the revenue.

On the contrary with all respect I entirely agree with the decision of the Madras High Court in the *Chengalvaraya Chetty v. Commissioner of Income-tax, Madras* (1). There what the assessee had done was this. He had originally bought some stock at Rs. 13-8-0 a piece, and for his financial year ending on the 12th April 1922 he put its real value down at the end of that year at Rs. 6 a piece. On that he showed a loss for that particular year and thereby I take it escaped assessment. But when it came to his return for the year beginning 13th April 1922 he did not put the stock at the real value of Rs. 6 a piece, but he inserted a fictitious sum of Rs. 13-8-0 a piece merely because that was what he

(1) 2 I.T.C. 14.

paid for it in the year before assessment. The result naturally was this that it enabled him to escape the tax on profits for the year beginning 13th April 1922. But what does Sir Murray Coutts Trotter say as to this: "The question is not so much of law but of business common sense. But there is a principle involved which determines the legal position, and I think the answer is clear that, as the value of the stock on the 13th of April 1922 was in fact and in truth Rs. 6 a piece, the assessee is not entitled to reduce what are truthfully called his profits by putting the fictitious value of Rs. 13-8-0 a piece on the stock-in-trade merely because that was the sum he happened to pay for it before the year of assessment. In my opinion, to allow this to be done would be to let the assessee ascertain not his profit or loss, but to debit himself with the same loss on the same goods *in toto* for perhaps a course of years. That cannot be permitted".

The present case seems to me to be the converse of the Madras case. It is not the assessee who is trying to put a fictitious value on the goods at the beginning of the year, but the Commissioner, who in effect has declined to allow the assessee to go into the question as to what was the true value of the goods in the beginning of the year. To my mind, it would be clearly wrong of us in this converse case to allow the Commissioner to put a fictitious value on the goods at the opening year, just as it was in the case of the assessee in the Madras case.

And I notice further that the formal answer which was returned by the Chief Justice at page 19 ran to this effect:—

"In our opinion the answer that we should return to the question is that the assessee, having elected in the previous year to value his stock at the market price of Rs. 6 a piece for the purpose of showing his trade loss during that year, is not entitled in the succeeding account to revert to the purchase price figure as representing the value of the goods, but is bound by the market price unless he can show that he made a mistake as to the market value."

It is therefore made plain in that case that if a mistake has been made it can be rectified. I do not read that word "mistake" as being confined to a mistake under the Contract Act. I think it would also cover an error. Here *ex hypothesi* there was an error made, *viz.*, that a wrong valuation was put on the stock at the beginning of the year as well as at the end of the year. In my judgment then both the errors should be corrected and not merely one.

Then there was something said in the course of the case about fraud and dishonesty and so on. Personally I regret that that was introduced into the discussion, because if any such odious charge are to be raised, they should be raised expressly so that the accused person may know exactly what he has to meet. Further there should be specific evidence on the point so that the Court itself may know what is the case before it. We have nothing of that sort here. So far as I am aware on the papers before us no such charge of fraud or dishonesty was made. At any rate when the matter came before the Commissioner he formulated no charges of dishonesty. Moreover he has by his counsel declined to allow us in the case before us to go into the figures of the balance sheets of the previous years. The case therefore is very different from the Madras case where the Commissioner laid before the Court all the material figures for the preceding years so that the Court could see precisely what had been done and precisely what was objected to by the Commissioner in that particular case.

The matter may further be tested by this that there are several clauses in the Act for protecting the public against frauds on the revenue. For instance, under section 28 there is power to the Commissioner to impose a penalty on an assessee who deliberately furnishes inaccurate particulars. But it is not suggested here that the Commissioner has attempted to do anything of the sort, or has served any such notice on the assessee, or that he has complied in any way with the provisions of the section which requires the assessee to be heard and to be given an opportunity of being heard before any such order is made. Similarly under section 52 certain false statements are to be treated as offences committed under section 177 of the Penal Code. Of course in addition to those penalties there is a provision made under section 34 for reopening assessments within a certain period of time. If that period of time expired then it may be that so far as the civil remedy is concerned, the amount in question cannot be recovered. But that would not necessarily apply to criminal proceedings.

The particular method of assessment which is now proposed by the Commissioner lends some support to the arguments of the appellants' counsel that what the Commissioner is really trying to do is not to recover the tax on the true profits for the year in question, but on the profits for the previous year or years which he is unable owing to lapse of time to recover under section 34. With that however we are not concerned. As I have already pointed out, the proper course is to determine the profits for the year ending the 31st December 1925.

There was one other point made at the end of the case, *viz.*, as to the position of the Commissioner under section 13. It is clear that *prima facie* the method of accounting adopted by the assessee is to be employed. On the other hand if the Commissioner is dissatisfied with it, and thinks that by that method the income cannot properly be deduced, then "the computation shall be made upon such basis and in such manner as the Income-Tax Officer may determine."

Now we have not got to determine whether the decision of the Commissioner is final if he does come to a particular determination on the proper method of assessing profits. This is because he has very properly, if I may say so, submitted to us by this reference what in law is the proper basis on which he should exercise his determination under section 13. It is on that footing therefore that we proceed to determine this case, and to state what in our opinion should be the proper basis to adopt.

As regards the formal question submitted to us I share the Commissioner's objections to its form. I also think that it goes beyond the real point for decision and is too generally stated to admit of an answer Yes or No being given without being exposed to a risk of misunderstanding.

Accordingly I would propose to give a limited answer so as to meet the real dispute in the present case. I would therefore reply as follows *viz.* "In the assessment of the Company for the year 1925-27 in respect of profits for the year 1925-26 the assessments Exhibits E and F ought to be varied by valuing at their true valuation the Company's stocks both at the beginning and at the end of the year in question and not only by revaluing the stock at the end of the year."

I wish to add some observations on the reference itself. I am very jealous of the reputation of the Bombay High Court, and I am very anxious that

the work we have to do in important cases should be done in the best possible way. This is not merely from any selfish motive, because all lawyers of experience know that the better the work is done by the Bar and by the solicitors down to their humblest clerk, the easier becomes the task of the Bench and the more likelihood is there of a correct decision being arrived at by that Bench, and also, I may say so with all respect, by any tribunal that may be superior to it. Bombay with its vast and growing commercial business is naturally attracting business of various sorts of a larger and more complicated nature. This in its turn results in greater complexity and importance in cases under the recent Income-tax Act of 1922 which itself is a far more complicated enactment than the one which existed previously, though I am happy to think that at present we have a less complicated Act to deal with than the Income-tax Act in England. But I will ask counsel for the Crown and the income-tax authorities to consider whether in these heavy cases involving lacs of rupees of public money, and for the matter of that, lacs of tax payable by private individuals or companies, it is not advisable to have the references submitted to the Court stated with all that precision and with all the relevant documents which a proper determination of the case requires. I think that in many respects the cases stated by the Income-tax Commissioners in England may be regarded as models of lucidity in what is admittedly a very difficult subject.

I will accordingly ask that each reference should be clearly stated, and that all relevant documents should be annexed to the petition so that we may know exactly what we have to deal with. It is not sufficient in my opinion merely to raise a general point of law. This Court is not a debating society. We give our decision on the cases that actually arise before us, and the practice of the Courts is to pay the closest attention to the facts of individual cases because it is only in that way and by testing the facts of a particular case and after hearing arguments, that the true principles of law may be elucidated and applied in any particular case. It is therefore of great importance that the Commissioner's findings of fact should be definite and adequate.

As regards the costs of this reference, we think they must be borne by the Commissioner as on the Original Side scale.

KEMP J.—This is a reference arising out of the assessment for the year 1926-27 ending the 31st March 1927 of the Ahmedabad New Cotton Mills Coy., Ltd., to income-tax and super-tax. The assessee whom I shall call the Company are taxed on the balance sheet ending the 31st December 1925, and it is with reference to that balance sheet that the question for our decision arises.

Shortly put, the opening balance of stock, according to the system of accountancy adopted by the assessee, is valued not at the cost price or the market value whichever was the lower but at what is described in the balance sheet as under cost. That is the first item on the debit side and as regards the closing stock balance on the credit side of the same account the valuation adopted by the Company is described as under cost. What the extent of the under cost is, is a matter which is not proved before us.

Shortly put, the Commissioner says that the assessee has in this balance sheet and in previous years assessed their stock balance at a value considerably below what it should be assessed at, and he claims that in the year under assessment the closing stock balance should be valued at a figure which he says is

its correct value. That the value he places on it is correct is admitted. But he objects to the opening balance being valued in a similar way.

The objections of the Commissioner are based, firstly, on the rule of accountancy under which he suggests that the closing balance of the previous year must be the same as the opening balance of the succeeding year. Consequently, as the assessee has adopted a particular valuation as the closing balance of the previous year that valuation must be adopted for the opening balance of the year in question.

It appears to me that no rule of accountancy can be invoked for the purpose of perpetuating an error in the balance sheet and if there be an error in the valuation of the opening balance for the year in question, there must be some way of correcting it in order to make the balance sheet a true one. Nor do I think that the case in *Chengalwaraya Chetty v. Commissioner of Income-tax, Madras* (1) has any application to the facts of this case, because what the assessee there was seeking to do was to take the opening rate of Rs. 13 of the prior year as the opening balance for the year for which he was being assessed. The opening balance in the year under assessment was not the correct closing balance of the previous year. Then it seems to me that if the principle contended for by the Commissioner were adopted, what would be valued for the year in question would not be the actual profits of that year, but it might very likely include profits which have been recovered the year before or in previous years, and to allow the Commissioner to now recover such profits in the way he claims would be practically to allow him to go behind the limitation provided by section 34 of the Act which enables the Commissioner to recover the profits which have escaped taxation provided he does so within a year of the termination of the year under assessment. It is to be noted that there are other methods by which any assessee who attempts to deliberately under-value his stock might be brought to book. They have already been referred to by the learned Chief Justice in his Judgment with which I respectfully agree.

Under the circumstances I am of opinion that the question referred for our opinion should be answered in the way suggested by the Chief Justice.

[243] IN THE HIGH COURT OF JUDICATURE AT BOMBAY.

Before Sir Amberson Marten Kt., Chief Justice and Mr. Justice Crump.

[5th March, 1928.]

The Trustees Corporation (India) Ltd.

Assessee.

v.

The Commissioner of Income-tax, Bombay

Referring Officer.

Income-tax Act (XI of 1922), Secs. 4, 10 and 24 (1)—Indian Company incorporated for dealing in shares—Agreement to purchase Burma Corporation shares—Price not paid in cash but in allotment of shares in Vendee company—Substantial difference between market value of shares purchased and face

value of shares allotted—Burma shares not delivered to Vendee company but resold by Vendors—Sale proceeds less than the face value of allotted shares in Vendee company—Claim of this deficiency as a trading loss by Vendee company—Vendee company, if entitled to take face value of its shares as purchase price of Burma shares—Loss, if capital loss.

The assessee, a private limited company promoted on the 10th February, 1920 by two English private companies, on the same date entered into an agreement with the latter for the purchase of a large block of shares held by them in Burma Corporation, Ltd., in consideration of allotting to the vendors an equal number of its own shares of the face value of Rs. 200 and in pursuance thereof allotted to them half its total number of shares. The English companies never handed any of the Burma shares to the assessee within the period of 3 years fixed for delivery and on the 14th November 1923 entered into a supplementary agreement inter alia providing for extension of the time for delivery by three more years, reducing the original purchase consideration by one half and giving them power to sell these shares with the assessee's consent, the sale proceeds together with dividends to be paid over to the assessee. In January, 1924, the Burma shares were accordingly sold in London by the English Companies at a price of Rs. 168 per share converted into rupees, the sale proceeds being kept by them as a deposit by the assessee. On an assessment to super-tax in respect of the dividends from Burma shares and interest amounting to over 20 lakhs, the assessee claimed to set off an alleged loss of about 50 lakhs from this sale, calculating this loss as the difference between the face value of its shares allotted and the sale price of Burma shares. The Income-tax authorities held that the assessee was not entitled to take the face value of its shares as the price paid for the Burma shares and that as the market value of the Burma shares on the date of the agreement to purchase was only Rs. 98-14/17, there was really no loss but a profit and further that the loss, if any, was a capital loss.

On a case stated by the Commissioner of Income-tax under section 66 (3) of the Act in compliance with the order of the High Court,

Held, (1) that having regard to the substantial difference between the nominal value of the shares given and the market value of the shares purchased, the assessee was not entitled to take as the price paid for the Burma shares the face value of its shares allotted in payment therefor and consequently there was no real trading loss to the assessee.

In re Wragg, Ltd., (1897) 1 Ch. 796, Followed.

(2) that having regard to the Memorandum of Association specifying the purchase of Burma shares and dealings in other shares as the objects of the assessee company, and to the fact of dealings in other shares as well, any loss if incurred by the assessee in the sale of Burma shares would be a revenue loss.

Commissioners of Income-tax v. The Melbourne Trust, (1914) A.C. 1001, Applied.

Case [Civil Reference No. 8 of 1926] stated under section 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bombay in compliance with the order of the High Court dated the 17th December, 1925 in Civil Application No. 871 of 1925.

CASE.

As required by the order of the High Court quoted above, I have the honour to submit under section 66 (3) of the Indian Income-tax Act, XI of 1922, (hereinafter referred to as the Act), for the decision of the Hon'ble the Chief Justice and the Judges of the High Court, the following question of law referred to in the said order arising out of the super-tax assessment for the year 1924-25 of the Trustees Corporation (India) Limited, (hereinafter referred to as the Petitioner Company):—

“Whether the Commissioner of Income-tax was not bound in law to take as the price paid for the Burma Corporation shares the nominal value of the shares allotted by the Petitioner Company in payment therefor.”†.

2. *Facts of the Case:* Early in the year 1920, two private English Companies by name “The Share Guarantee Trust Limited” and “The Inter-Continental Trust Limited” (hereinafter referred to as the two English Companies) formed a private Indian Company styled the Trustees Corporation (India) Limited which is the petitioner Company. Its super-tax assessment for the current financial year has given rise to this reference. The chief object of its formation was to take over from the two English Companies a huge block of shares (numbering 3,12,817 in all) of the nominal value of £1 each in the Burma Corporation Limited. It was incorporated on 10th February 1920 and the above two English Companies were its sole proprietors. They possessed all its 1,60,711 issued shares of the nominal value of Rs. 200 each excepting three.

3. By agreement dated the 10th February 1920 (copies enclosed, Exs. A* and B*), the two English Companies agreed to sell to the Petitioner Company which in return was to allot to the two English Companies an *equal* number of its own shares of the nominal value of Rs. 200 each. By two other agreements made on the same day *viz.*, 10th February 1920 (copies submitted herewith Exs. C* and D*), it was further *inter alia* agreed that the Petitioner Company should allot immediately one half of its shares forming the above purchase consideration, the remaining one half being allotted at the rate of one share in the Petitioner Company for each two shares in the Burma Corporation Limited.

4. In the first two agreements (Exs. A and B), it was further laid down that in case the Burma Corporation shares of 1-£ each were, prior to the completion of the purchase, exchanged for shares in the Burma Corporation (India) Limited of Rs. 10 each at the rate of 14 such shares of Rs. 10 each to one of 1-£ each in the Burma Corporation Limited, in place of each 1-£ share, 14 shares of Rs. 10 each in the Burma Corporation (India) Limited, were to be exchanged for each share of Rs. 200 in the Petitioner Company.

5. From the above, it will be clearly seen that the Petitioner Company paid absolutely nothing in cash to the two English Companies for the Burma Corporation shares sold to it. It was merely to allot an equal number of its own shares of the nominal value of Rs. 200 each. It was all a sort of family arrangement. The two English Companies being also the sole pro-

*Not printed.

prietors of the Petitioner Company were really the vendors as well as the purchasers of the above Burma Corporation shares.

6. In accordance with the above agreements on the 11th February, 1920, the Petitioner Company allotted half the total number of the shares to be given as the purchase price *i.e.*, 1,56,408 of its shares to the two English Companies. The Burma Corporation which was an English Company was thereafter converted into an Indian Company styled the "Burma Corporation (India) Limited." It was registered at Rangoon and 14 shares of the face value of Rs. 10 in it were given in exchange for each original share of the nominal value of £1. That is to say, for the 3,12,817 shares of £1 each, fourteen times this number *i.e.*, 43,79,438 shares of the nominal value of Rs. 10 each were given.

7. The two English Companies never handed a single share either of the Burma Corporation Limited, or the Burma Corporation (India) Limited, to the Petitioner Company and so, as the condition was to allot 1 share of the Petitioner Company for two shares in the Burma Corporation Limited, or 28 shares in the Burma Corporation (India) Limited, no further allotment was made in favour of the two English Companies by the Petitioner Company. On the 14th November 1923, the two English Companies executed fresh agreements with the Petitioner Company (Exs. E* and F*) whereby they agreed to forego half the number of the shares which were to be allotted in exchange for the shares in the Burma Corporation and accepted the above allotment of 1,56,408 shares in full settlement of the purchase price for their 3,12,817 Burma Corporation shares of 1-£ each or 43,79,348 shares of Rs. 10 each. Thus the ultimate result was that for its 1,56,408 shares of the face value of Rs. 200 each, the Petitioner Company was supposed to have received 43,79,438 shares of Rs. 10 each in the Burma Corporation (India) Limited. Though these shares were alleged to have been sold in 1920, they were never delivered to the Petitioner Company as stated above. They were retained by the two English Companies and shortly after the execution of the second agreement of November 1923; they were all sold away in England at 8s. each by the two English Companies acting as alleged under instructions from the Petitioner Company. They realised £1,751,775—4—0 = Rs. 2,62,76,628 at 1s. 4d per Re., which sum was kept by the two English Companies with them as a deposit from the Petitioner Company and not sent to India.

8. When the above sale was effected, the Petitioner Company worked out an imaginary loss on the transaction as under:—

	Rs.
Purchase price paid <i>viz.</i> , 1,56,408 shares in the Corporation of the face value of Rs. 200 each, Rs. 1,56,408	
× 200	.. 3,12,81,600
Sale Receipts.	.. 2,62,76,628
	<hr/>
Net loss.	.. 50,04,972
	<hr/>

The Petitioner Company had net income from dividends from the Burma Corporation shares and from interest amounting to Rs. 20,14,259 and it wanted to set off the above loss against this income and get exemption from the tax.

9. The Senior Income-tax Officer, Bombay, declined to allow the loss on the ground that it was capital loss and assessed super-tax amounting to Rs. 1,22,766, income-tax having been already deducted at source.

10. The Petitioner Company thereupon lodged an appeal with the Assistant Commissioner of Income-tax, Bombay, who considering that there was really no loss in the above transaction but a huge profit, declined to interfere. A revision petition was then preferred by the Petitioner Company to the Commissioner of Income-tax under section 33 of the Act. He too declined to interfere.

11. The Petitioner Company thereafter wanted a reference to the High Court. It was therefore called upon to state definitely the points on which it desired a reference. In reply it sent a draft reference, in which *assuming that there was a loss*, it wanted the High Court to decide whether it was allowable or not. The order (Ex. G*) was thereupon passed. Therein it was stated that as the only question which had arisen out of the decision of the Assistant Commissioner of Income-tax (Ex. K*) was one of *fact, viz.*, the actual amount of profit or loss resulting from a certain transaction, no reference could be made to the High Court. To avoid any misunderstanding, the case was reviewed at full length by the Commissioner in that order and the probable profit on the transaction *viz.*, Rs. 1,04,35,828 worked out and a copy of it sent to Messrs. Ferguson & Co., Chartered Accountants, who represented the Petitioner Company in connection with this assessment. They were informed that unless the point of law involved was specifically pointed out, no reference could be made to the High Court.

12. In the above order (Ex. G), it was made clear that the method whereby the loss of Rs. 50,04,972 was worked out by the Petitioner Company was fallacious and instead of there being a loss, the Petitioner Company appeared to have made a large profit. Messrs. Ferguson & Co., sent their reply on the 13th August (Ex. H*) in which instead of taking the allotted shares at their nominal value of Rs. 200 each they followed the Commissioner's method of calculating the profit or loss from the transaction and worked out a fresh loss of Rs. 45,35,748 in place of the original loss of Rs. 50,04,972. The difference between their result and the Commissioner's result was due to their assumption that as ultimately, in 1923, it was decided to accept the 1,56,408 shares allotted on 11th February 1920 in full payment of the purchase price of the 3,12,817 shares of £ 1 each of the Burma Corporation Ltd., while calculating the probable market value of the allotted shares on 11th February, 1920, it should be assumed that one share in the Petitioner Company was worth two shares in the Burma Corporation on that date. The Commissioner in his calculations took one share in the Petitioner Company as worth only one share in the Burma Corporation on 11th February 1920 as that was actually the case on that day. He took the probable market value of the allotted shares at Rs. 98-14/17 each and the Accountants wanted him to take it at twice that figure or Rs. 197 on the above assumption.

13. In his reply dated the 24th August 1925 (Ex. I*), the Commissioner pointed out the fallacy in the assumption that on 11th February 1920 one share in the Petitioner Company was worth two shares in the Burma Corporation Ltd.

14. Then the Solicitors of the Petitioner Company wrote the letter (Ex. J*) wherein the method of calculation adopted by the Accountants in their above letter of 13th August (Ex. H) was given up and the original argument of taking the value of the shares allotted at Rs. 200 each (the face value) was once more taken up and the Commissioner was requested to refer the question set out in para 1 above to the High Court.

15. The Solicitors were thereupon informed that no reference could be made on such a point as it involved no question of law. They then applied by their petition dated the 14th October, 1925 to the High Court requiring the Commissioner to state a case for the opinion of the High Court in regard to the assessment of their clients to super-tax. The High Court was then pleased to order a reference to be made to it under section 66 (3) of the Act.

16. The question for decision by Your Lordships is categorically stated in para 1 above. As section 66 requires me to state my opinion while forwarding the reference, it is given in the following paragraphs:—

17. *Opinion of the Commissioner:* In this case, it is to be determined whether the law requires that when the purchase price of a certain thing is not paid in cash but by allotting shares in a company, we should take into account the "nominal value" of the shares allotted or their market value to ascertain the cash equivalent of the purchase price paid. The dispute relates to the probable amount of profit or loss from the sale of certain shares and in order to arrive at the same we have to deduct the sale price realised from the purchase price paid for these shares. We know the actual sale price realised. We do not know the purchase price which is stated to be 1,56,408 shares in the Petitioner Company of the "nominal value" of Rs. 200 each. We have therefore to calculate first of all the value in cash of these allotted shares to know the profit or loss from the sale transaction in dispute. The Petitioner Company contends that the law requires that the cash value of each of the allotted shares is to be taken to be its "nominal value" viz., Rs. 200. It is to be seen whether this is correct or otherwise.

18. The ordinary meaning of the word "nominal" when used with reference to the value or price of a thing is "existing in name only, not real or actual" as given in the Concise Oxford Dictionary. "Nominal value" means "value which is not real or actual." Therefore if we take into account the "nominal value" (i.e., value which is not real but imaginary) of the shares allotted, the purchase price which we will thus arrive at will be an imaginary and fictitious figure. Taking into account an imaginary and fictitious purchase price while calculating the profit or loss from the sale transaction, will result in our arriving at not the real or true profit or loss but some imaginary fictitious figure. Now we have to see whether the Income-tax law requires us to tax real and true profits or imaginary and fictitious ones.

19. That the Legislature can deliberately enact a statute requiring tax to be paid on imaginary incomes and profits is a sufficiently startling proposi-

tion to make us look for the clearest language in the Act expressly authorising action of this kind. Nothing can be more atrocious than asking a man to pay tax on what he never earned and nothing can be more unjust to honest taxpayers if real profits are allowed to be converted into imaginary losses by an Act of the Imperial Legislature. Now taking up the Income-tax Act of 1922, Your Lordships will find that its Chapter I deals with the "Charge of Income-Tax." Its section 3 enacts that tax shall be paid "in respect of all income, profits and gains of the previous year of every individual, Hindu Undivided family, Company, firm, etc." Then follows section 4 which lays down that "the Act shall apply to all income, profits and gains as described or comprised in section 6, from whatever source derived, accruing or arising, or received in British India, or deemed under the provisions of the Act to accrue or arise or to be received in British India". These sections clearly contemplate levying tax on real income, profits and gains and not imaginary ones. What is to be taxed must be real income, profits and gains with the condition that these do accrue or arise or be received in British India. If they do not accrue or arise or are not received in British India, there must be some express provision in the Act under which they can be deemed to have accrued or arisen or been received in British India. The important point to notice in this connection is the fact that these sections do not suggest levying tax on what may not be income, profits and gains but may be deemed to be so under the provisions of the Act. Just as in these charging sections there is an express reference to the provisions in the Act under which income, profits and gains which do not actually accrue or arise or are not received in British India are to be deemed to so accrue or arise or to be so received, in case there were any provisions in the Act under which that which did not constitute real income, profits and gains was to be deemed to be so, they would most certainly have been referred to in these sections. The whole scheme of the Act is to tax nothing but real and true income, profits and gains. This is the reason why in the case of tax deducted at source on "salaries" and "interest on securities" under section 18 of the Act, a refund is claimable under section 48 taking into account the actual total income of the previous year. This is also the reason why under section 24 of the Act loss or profit and gains in any year under any one of the heads mentioned in section 6 is allowed to be set off against the income, profits and gains under any other head.

20. Now turning to Chapters V and V-A of the Act, Your Lordships will see that they relate to "Liability in special cases" and if anywhere any special provision *re*: taxation of imaginary income, profits and gains did exist in the Act, it ought to have found a place in these Chapters. In Chapter V section 42 (2) expressly enacts that where owing to certain reasons the accounts are so manipulated that the real profit is not disclosed, the Income-tax Officer is to levy tax on what may be the actual profits or may reasonably be deemed to be the actual profits. This is significant as clearly showing that fictitious profits are not the subject matter of taxation under this Act and that where they are suspected to be so, an attempt to tax the real profits should be made.

21. Turning to Chapter V-A, Your Lordships will perceive that section 44-B lays down that in the case of certain shipping profits, the taxable income be in the first instance deemed to be 5 per cent of the total amount paid or

payable on account of the carriage of passengers, live-stock and goods by the ships concerned. As this is taxing what may be an imaginary profit, section 44-C at the same time expressly lays down that in the following year when the actual profit is known, an adjustment of the tax thus paid can be made by levying tax on the actual income.

22. Super-tax is nothing but an additional duty of income-tax as laid down in section 55 of the Act which enacts that it is, like income-tax, payable on "the total income of the previous year". Section 56 lays down that the total income for income-tax purposes is to be taken to be the total income for super-tax purposes. Whatever is said in the preceding paragraphs about income-tax applies word for word to super-tax too.

23. As far as the Income-tax Law is concerned, I feel no hesitation in saying that there is nothing in the Act which requires "nominal" values and "nominal" profits to be taken into account. We have to tax only the actual and real income, profits and gains.

24. That the "nominal" value of a share in a company cannot be the same as its intrinsic value except by accident needs hardly any demonstration on my part as every one knows that a share may be worth ten times as much or only one-tenth of its nominal value. The financial position of a company, and the rate of dividends it is paying have much to do with the intrinsic value of its shares.

25. Enough has been said above to show that the Act does not lay down that we are to take into account the nominal value and thereby work out imaginary profits or losses, taxing those who should not be taxed and letting go those who should pay tax. We must take only the intrinsic values into account and arrive at the real profit or loss which alone is to be considered for the purposes of the Act.

26. The next point to be considered now is whether there is anything special in this case requiring the intrinsic value of the allotted shares to be taken to be equal to its "nominal" value. The Petitioner Company does not put forward any such claims. However, we might for the sake of justice, as well consider it. The facts to be borne in mind in this connection are that the two English Companies who sold the Burma Corporation shares were themselves the sole proprietors of the Petitioner Company which purchased them, that each share in the Burma Corporation was worth only Rs. 98-14/17 on the day on which the purchase took place as admitted by Messrs. Ferguson & Co., on behalf of the Petitioner Company (vide Ex. H) and that documents were executed by the two English Companies whereby the Petitioner Company was made to allot to the two English Companies shares of the nominal value of Rs. 200 in exchange for the above shares worth Rs. 98-14/17 only. We have thus a transaction in which the vendors and the purchasers are in reality one and the same party and which purports to exchange a thing worth Rs. 98-14/17 only for something which we are asked to value at Rs. 200. Would it be at all justifiable to do so under any circumstance whatsoever? *Prima facie* if the transaction is to be supposed to be *bona fide*, all that we can do is to take it that as reasonable and sane beings, those who purchase the shares worth Rs. 98-14/17 only paid for them only Rs. 98-14/17 and nothing more. Why should the Petitioner Company pay a pie more for what was

worth not more than Rs. 98-14/17? If it did pay anything more, it was nothing but a pure gift given because it mattered not, the donor and the donee being in reality one and the same party as observed above. The parties might as well have exchanged a lead pencil worth As. 2 for a gold watch worth Rs. 100 and tried to make us believe that the pencil was worth Rs. 100, or that the watch was worth only 2 annas! The only reasonable inference in a case of this kind is that the shares were worth only Rs. 98-14/17 to the Petitioner Company and so it agreed to give them away in exchange for shares worth Rs. 98-14/17. They could not have been worth Rs. 200. Else they would not have been parted with for what was worth Rs. 98-14/17 only as everybody knew at the time. The intrinsic value cannot thus be supposed to have been in any case equal to the nominal value.

27. Where the relations between the parties are such as to render possible transactions of this kind we find in this case and where the cash value of an asset given in exchange is not known, the best course to ascertain it is to find out how much it would fetch in the open market. Here is a Company. On the 11th February 1920, it has no assets whatsoever except certain shares in the Burma Corporation plus Rs. 400 paid in cash for three of its shares minus the preliminary expenses of floating the Company. Its prospects depend on the prospects of the Burma Corporation shares alone. Could its shares be in any way regarded as superior to the Burma Corporation shares themselves? A would-be investor would rather pay Rs. 98-14/17 for a Burma Corporation share than this much amount for a share in the Petitioner Company, because his investment in the latter Company would be saddled with the extra expenditure of managing it and the yield would thus certainly be less than what could be had by investing direct in the Burma Corporation shares. The Petitioner Company, of course, in its prospectus makes mention of dealing in other shares etc., but that would really mean nothing to would-be investors as long as they saw that the Company had got in return for all its issued shares but three, shares in the Burma Corporation only. It is doubtful whether any one in the open market would have paid even Rs. 98-14/17 for these shares on the 11th February 1920.

28. The issue of shares of a certain nominal value does not mean that the shareholder has a right at any time to claim from the Company the "nominal" value of the shares. Were it so, we would be bound to take it that the Petitioner Company really paid Rs. 200 when it allotted a share. All the claim that a shareholder has on a Company is to have a share in the profits, and in the assets of the Company, when wound up, proportionate to the number of shares held by him. This is all that he gets and the market value of a share represents the cash value of these benefits. The market value alone can represent the value of a share in cash thus.

29. If there were any law under which the "nominal value" of a share is to be taken as its cash value, all that a debtor need do is to form himself into a company and pay his creditors by issuing shares of any nominal value he likes. No one but himself would accept such shares at the nominal value and that would not in the least mean that they were worth their nominal value in reality. It would be all a fictitious transaction.

30. Before concluding, I invite the attention of Your Lordships to the letter of 13th August last (Ex. H) of the Chartered Accountants who repre-

sented the Petitioner Company in the matter of this assessment. In that letter, they agreed that the price of the Burma Corporation shares on the 11th February 1920 was Rs. 98-14/17. They, however, wanted that on that day one share in the Petitioner Company should be taken to have been allotted not for one share in the Burma Corporation but two as per the agreement made in 1923. How can this be done? No one on the 11th February 1920 knew what was going to happen in November 1923. On the 11th February 1920, the shares allotted became the property of the two English Companies. Any appreciation or depreciation thereafter was theirs. If in 1923 their value was doubled, it was their profit. It cannot mean that the Petitioner Company paid twice the price it actually paid on 11th February 1920. On that day it allotted one share deliberately for one share in the Burma Corporation worth Rs. 98-14/17 only.

31. For all the above reasons, my opinion is that the Commissioner is not bound to take as the price paid for the Burma Corporation shares the "nominal" value of the shares allotted by the Petitioner Company in payment therefor.

32. A copy of the decision of the High Court may kindly be certified to me for further action as required by section 66 (5) of the Act. On its receipt as this transaction appears to have taken place entirely outside British India, the next question for consideration will be whether its result can be taken into account in ascertaining the income liable to tax here in view of the provisions of section 4 (2) of the Act.

SUPPLEMENTAL CASE.

Pursuant to your Lordships' interlocutory judgment delivered on 5th October last in the above matter, I submit herewith for favour of opinion, additional questions of law which arise in this case. As observed in his judgment by the learned Chief Justice, the Commissioner was merely required to refer a specific question to the High Court under the order issued by it on 17th December 1925 and that had to be done. However, in the last para of the Reference made in obedience to that order, I had added that on receipt of your Lordships' opinion on the specific question submitted for opinion, the next point for consideration would be whether the profit or loss arising from the transaction could be taken into account in view of the provisions of section 4 (2) of the Act. Your Lordships having now given me "a general liberty to amend the case stated" I have considered it advisable to submit for the opinion of the Hon'ble Court, all the questions which arise in the case and which must be authoritatively settled before it can be finally decided. These have been categorically set out in the following paragraph.

2. *Questions for the opinion of the High Court:*—Including the question already referred as per the original Reference No. Ref. 7 of 27—3—1926, the following three questions are submitted for favour of your Lordships' opinion:—

(1) Whether the Commissioner of Income-tax was not bound in law to take as the price paid for the Burma Corporation shares, the nominal value of the shares allotted by the Petitioner Company in payment therefor.

(2) Whether the alleged loss in question, if any, was capital loss or revenue loss, and

(3) Whether the alleged loss in question, if any, can be taken into account in view of the fact that it has accrued and arisen outside British India, in view of the provisions of sections 4 (1) and (2) of the Income-tax Act, 1922.

3. *Facts of the Case*:—The facts of the case have been already stated in paras 2 to 16 of the original Reference made on the 27th March last and they need not be recapitulated here therefore. Exhibits A to K referred to in this present Reference are those accompanying the original Reference. Fresh exhibits now submitted are marked L to U*.

4. *Opinion of the Commissioner*:—As regards question No. 1, the Commissioner's opinion is already given in paras 17 to 31 of the previous Reference dated the 27th March. However, since His Lordship the learned Chief Justice has been kindly pleased in the last para of his judgment to allow me leave to state my views on any matter appearing in his interlocutory judgment of 5th October last and as I am invited to "put in figures showing the price per share" of the Burma Corporation in 1920 and the price realised in 1923 and to "make a corresponding statement as regards the figures put forward by the Petitioner Company", I venture to make below a few additional observations *re*: this question.

5. It was on 10th February 1920 that agreements were first made between the two promoter companies and the Petitioner Company (Exs. A, B, C and D) whereby one share in the Burma Corporation Limited of the face value of 1 £ (or 14 shares of the Burma Corporation (India) Ltd. of Rs. 10 each when issued in exchange for each of these 1 £ shares) was to be exchanged for one share in the Petitioner Company of the face value of Rs. 200. The market value of this 1 £ Burma Corporation share that day was 14£ and as the rate of exchange that day was 2s. 10d. per rupee, 14 £ were equivalent to Rs. 98-14/17 as admitted by Messrs. A. F. Ferguson & Co., Chartered Accountants, on behalf of the Petitioner Company in their letter of the 13th August 1925 (Ex. H). Thus each share of the Burma Corporation was at the time of exchange worth Rs. 98-14/17 only as already pointed out in the previous Reference. Hence the agreements of 10th February 1920 purport to allot one share in the Petitioner Company of the face value of Rs. 200 for one share in the Burma Corporation of the market value of Rs. 98-14/17. This is self-evident and needs no further proof.

6. Now, my Lords, I am highly obliged to the learned Chief Justice for drawing my attention to the English cases bearing on this point, especially the case *In Re Wragg Limited*, (1). I have carefully gone through the judgments in these cases and will feel extremely grateful if your Lordships take into account in deciding this question, the very weighty words of Lord Justice A. L. Smith (at pages 835 and 836) in his judgment in the above case of *Wragg Ltd.* He states as under (page 835):—

"It is now well settled law that for a share-holder in a company limited by shares to have fully paid up shares, and therefore not to be liable for calls

*Not printed.

(1) (1897) 1 Ch. 796.

in a winding-up of the company, he must show that he has fully paid up to the face value of the shares, either in cash or in value received by the Company in some form; or partly in cash and partly in value received by the company in some form; and if the payment other than in cash be relied on, this can only be so if there be a 'contract duly made' in writing and filed with the Registrar of Joint Stock Companies, at or before the issue of the shares, pursuant to section 25 of the Companies Act, 1867. The House of Lords has definitely settled this point in the case of the *Ooregum Gold Mining Co., of India v. Roper*.⁽¹⁾ 'Partial payment is not sufficient; but shares may be lawfully issued as fully paid up for considerations which the company have agreed to accept as representing in money's worth the nominal value of the shares'; per Lord Watson in the *Ooregum Case*.⁽¹⁾

Then follows at page 836, the most important part in this judgment which covers exactly the present case before your Lordships. It is as under:—

"Again, if in a registered contract, a money value less than the face value of the share be placed upon the consideration which the company had agreed to accept as representing in moneys' worth the nominal value of the share, that share, I should think, would not be fully paid up; for instance, as was put in argument, a contract to supply to a limited company 100 tons of coal, valued at 10s. per ton, as a consideration for 100 1-£ shares—these shares would not be, I think, fully paid up.

"There would be no necessity in such a case for impeaching the agreement, for that the shares were not fully paid up in money or money's worth would be apparent upon its face. Cotton L. J. in *In Re Almada and Tirito Co.*,⁽²⁾ points to such a case as this, though he did not decide it".

Now, my Lords, what do we find in this case? As per the above judgment, the two promoter companies must show that they have "fully paid up to the face value of the shares either in cash" or in kind in order to escape liability for calls in a winding up. Do they show this? The only thing that they can point to is that in return for a share of the face value of Rs. 200, all that they gave was a promise to hand over a share in the Burma Corporation of the then market value of Rs. 98-14/17. This is all that the agreements of 10th February 1920 go to establish. (What the price of a Burma Corporation share was on 10th and 11th February 1920 was known to every one. There is no need at all to specify in an agreement the price of a share quoted in the share market from day to day). Thus there is absolutely no difference between this case and the case cited by Smith L. J. of a contract to allot a 1-£ share in a company in return for a ton of coal valued at 10s. As stated by him, in such a case the fact "that the shares were not fully paid up in money or in money's worth" or "in meal or in malt" [in the words of Lord Justice Gifford in *Drummond's case*,⁽³⁾] is apparent upon the very face of the agreements made and there is no necessity to impeach them even, to establish the fact that the shares in this case were issued at a discount. This is self-evident, as instead of being exchanged for Rs. 200 in cash or kind, the promise of a consideration worth only Rs. 98-14/17 on the date of the agreements was accepted per

(1) (1892) A.C. 125.

(2) (1888) 38 Ch.D. 415.

(3) (1869) 4 Ch. 772.

share. It passes one's belief that such an extraordinary transaction could have taken place but when we bear in mind the fact that the vendors and the purchasers of these Burma Corporation shares were in reality one and the same party, the two promoter companies who sold these shares to the Petitioner Company being the sole owners of the latter having, at the time of its formation, all its issued shares numbering 1,60,710 excepting two, your Lordships will easily see how such a transaction came to pass. Even in a winding up, in accordance with the judgment of Smith L. J. in the above case, there could be no obstacle to holding the two promoter companies liable to contribute the difference between Rs. 200 and Rs. 98-14/17.

7. I fully admit, my Lords, that where the assets taken up in exchange for shares allotted cannot, from the nature of them be said to have any market value *e.g.*, livery stables, goodwill, live stock, carriages, harnesses, etc., as in the case of Wragg Limited, the estimate by the contracting parties of the value of the assets taken up "ought not to be critically examined" as stated by Lord Watson in the *Ooregum Case*(1). In the case of *Wragg Limited*, (2) in the words of Rigby L. J. (at page 839) "the assets (notably the goodwill of the business) could not from the nature of them be said to have any market value; and what they would be worth to a company incorporated to carry on the business would depend upon considerations as to which there would be room for considerable honest difference of opinion". In the present case, however, there can be no honest difference of opinion whatsoever as to the market value of the assets taken up *viz.*, shares in the Burma Corporation. It was Rs. 98-14/17 per share without any doubt and in such a case no Court can assume that it was full payment for a share of the face value of Rs. 200. When the consideration given per share allotted was worth only Rs. 98-14/17 on the face of it, how can any one hold that there was full payment in kind, if not in cash, to the extent of Rs. 200 for the shares issued by the Petitioner Company? To allot a share of the face value of Rs. 200 in return for a share worth Rs. 98-14/17 is undoubtedly issuing shares at a discount. A liability to pay Rs. 200 less Rs. 98-14/17 would in that case attach to the shareholders of the shares allotted, in a winding-up proceeding.

8. In the foregoing discussion, I have assumed for the moment that in calculating profit for income-tax purposes, we are bound by decisions issued under the English Companies Act applying to winding up and similar proceedings regarding companies. I will now invite your Lordships' attention to a few decisions under the English Income-tax Acts which indicate that whatever may be the case in winding up and similar proceedings, the proper method of determining liability to income-tax in cases of this kind, where shares are issued in exchange for assets taken up, is to take into account the intrinsic and not the face value of the shares issued in order to ascertain the profit liable to the tax. Justice Rowlatt who is an acknowledged authority in England on income-tax matters, in his judgment in the case of *Collins (Inspector of Taxes) v. The Firth Brearley Stainless Steel Syndicate, Ltd.*, (3) delivered in March 1925 in the High Court of Justice, King's Bench Division, says:—"Now the only items that I have to deal with are the sale of the American patent for a consideration in shares and what will have to be done there is

(1) (1892) A.C. 125.

(3) 9 Tax Cas. 520.

(2) (1897) 1 Ch. 796.

to ascertain as best you can—it may not be easy—what this patent really cost the company, and secondly what these shares were worth when they were taken over as the price of the patent, and the difference is the profit". The company concerned in the above case had paid for the American patent referred to by Justice Rowlatt and some other patents by issuing its shares of the face value of £23,000 as fully paid. It sold the patents for 550 shares of 100\$ each to another company and Justice Rowlatt gave his opinion as above as to how to calculate profit for income-tax purposes in such a case. He has not recognised any such dictum as we are asked by the Petitioner Company to accept in this case *viz.*, that the Commissioners of Income-tax were bound to take the face value of the shares concerned in ascertaining the profits liable.

9. In the case of the *Californian Copper Syndicate Ltd. v. Harris*(1), in the Court of Exchequer (Scotland), Second Division, it was held that the difference between the purchase price and the *value of the shares for which the property concerned was exchanged* should be taken as profit liable to tax.

10. The only way to arrive at true profits is by taking into account the intrinsic and not the face value of shares where they form part of the consideration for sale or purchase. As stated in the previous Reference, the intrinsic value of the shares issued by the Petitioner Company cannot have exceeded Rs. 98-14/17 on the day they were issued as fully paid up as the assets that day were hardly anything beyond an equal number of shares of the Burma Corporation received in exchange—(*vide* para. 27 of the previous Reference).

11. Though on 11th February 1920, 1,56,408 shares were issued by the Petitioner Company to the two promoter companies, the latter never delivered a single share of the Burma Corporation Ltd., in return. For full three years and nine months, nothing was done. Then, by agreements dated 14th November 1923 (Exs. E and F), it was agreed to extend the period of the delivery of the Burma Corporation shares up to February 1923, the two promoter companies agreeing in return to deliver in all 33,12,817 shares in the Burma Corporation of 1£ each instead of only 1,56,408 shares as originally agreed, in return for the consideration already received on 11th February 1920. Hence, the ultimate result was that for one share in the Petitioner Company issued on 11th February 1920, 2 shares in the Burma Corporation of 1£ each or 28 shares in the Burma Corporation (India) Ltd., of Rs. 10 face value were to be delivered to it. These twenty eight shares, when sold, realised 8s. or Rs. 6 each. Hence for each share in the Petitioner Company issued on 11th February 1920, Rs. 168 were received by it when the 28 shares in the Burma Corporation (India) Ltd., received in exchange were sold. Now, as shown above, each share in the Petitioner Company, on 11th February 1920 when it was issued was worth Rs. 98-14/17 only. Hence, for Rs. 98-14/17 it got Rs. 168 in 1923. Thus there was a clear profit of Rs. 69-3/17 per share issued by the Petitioner Company. It admits that Rs. 168 were realised in return for every share issued on 11th February 1920 but contends that what it paid was Rs. 200 which was the face value of the shares issued and not Rs. 98-14/17 as contended on behalf of the Crown. Hence, according to it there was a loss of Rs. 200 less Rs. 168 or Rs. 32 per share. As your Lordships have

expressly asked me to state this very plainly to avoid confusion, I put it as under for the sake of clearness.

Price paid on 11th February 1920 per every two shares of the Burma Corporation Ltd., by the Petitioner Company (as per agreements Exs. A & C read with Exs. E and F).		Price realised per every two shares of the Burma Corporation or twenty-eight shares of the Burma Corporation (India) Ltd.	
According to the Petitioner Company.	According to the Commissioner.	According to the Petitioner Company.	According to the Commissioner.
Rs. 168	Rs. 98-14/17	Rs. 200	Rs. 168

Thus it will be seen that the only difference between the Commissioner's calculations and those of the Petitioner Company is as regards the purchase price. The Petitioner Company contends that it should be taken at the nominal value of its shares *viz.*, Rs. 200. The Crown contends that the nominal value cannot be taken in this case and that the Petitioner Company has received only Rs. 98-14/17 for each of its 1,56,408 shares issued as purchase consideration leaving a liability of Rs. 101-3/17 on the two promoter companies. The total purchase consideration being 1,56,408 shares, the Commissioner contends that a profit at the rate of Rs. 69-3/17 per share issued has been made. The Petitioner Company, on the other hand, claims a loss of Rs. 32 per each of these shares. I trust these figures will make matters clear. Though, under the original agreements of 10th February 1920, the Petitioner Company was to allot 1,55,408 more shares on account of the purchase consideration, that was given up in 1923 under the agreements made on the 14th November 1923 (Exs. E and F) because both the promoter companies failed to deliver within three years the Burma Corporation shares as required under the original agreements of 1920 and because the Petitioner Company agreed to give them 3 years more for their delivery. Thus the total purchase consideration consisted of the 1,56,408 shares originally allotted on 11th February 1920. Had more shares been allotted as purchase consideration, we would certainly have taken the additional number into account valuing them as best as we could (in the words of Justice Rowlatt) in the very extraordinary circumstances of the case. As no more shares were allotted we have not got to value them to make matters more complex.

12. In view of your Lordships' remarks as to whether the whole of this scheme of the two promoter companies was illusory or otherwise, I beg permission to go through the agreements Exs. A, B, C, D, E and F in detail here to give your Lordships some material to arrive at some definite conclusion on this point. To start with, Exs. A and B (para 3) require the Petitioner Company to exchange its shares of the nominal value of Rs. 200 for an equal number of shares in the Burma Corporation Ltd., of the market value of Rs. 98-14/17 which in itself is a most extraordinary proceeding. Exs. C and D provide that though the Petitioner Company was to allot 1,56,408 of its shares at once, it was not to be given the consideration for them *viz.*, an equal number of the Burma Corporation shares forthwith, but only 25,000 shares

were to be handed over at once and the remaining 1,31,408 shares were to be handed over within the next three years. In the meanwhile, the two promoter companies were free to "deposit and charge and/or continue the deposit and charge of such shares with Lloyds Bank Ltd., or any other Bankers as security for any liability or liabilities" of the promoter companies to the extent of 5 million pounds sterling! It was further provided that the promoter companies should have the power to sell these shares with the assent of the Petitioner Company and utilise the sale proceeds in discharging their liabilities, remitting to the Petitioner Company what was not required for that purpose. The period of 3 years mentioned in these four agreements (Exs. A to D) expired on 9th February 1923. Not a single share was, however, delivered as per these agreements. The Petitioner Company having allotted on 11th February 1920, 1,56,408 shares, was not given even a pie of the promised consideration for over 3 years and thus the agreements made were not observed at all. Surely this is most extraordinary. Though the three years expired on the 9th February 1923, nothing whatever was done till 14th November 1923 when the agreements Exs. E and F were executed in which the period for the delivery of the Burma Corporation shares was extended up to 10—2—1926 and the two promoter companies agreed to forego half of the purchase consideration as originally fixed in view of these fresh agreements giving 3 years more for the delivery of these shares. The two promoter companies also agreed to pay to the Petitioner Company the proceeds of the sale of these shares when sold. To the last, however, not a single share was handed over and in January 1924, the shares were sold by the two promoter companies, one of them *viz.*, the Intercontinental Trust *itself re-purchasing* 3,79,439 shares of Rs. 10 each in the Burma Corporation (India) Ltd., which represented 27,102-11/14 original £1 shares in the Burma Corporation Ltd., sold by it to the Petitioner Company. (vide Ex. L deposition of Mr. Sandeman, one of the directors of the Petitioner Company). Even then the money realised by the sale was not paid over to the Petitioner Company. It was kept by the two promoter companies as a deposit from it. Thus, from one end to the other, we come across nothing but a most extraordinary set of circumstances and the only possible explanation for these which suggests itself to me is that the whole scheme was illusory and set up by the two promoter companies for reasons which, however obvious, need not be discussed here. Not only have shares been issued at a discount originally but not a pie of the consideration for them was handed over for nigh 4 years, the shares which were to be given in exchange having been kept by the promoter companies with themselves for their own business purposes. We are, my Lords, asked not only to take the purchase consideration at the full nominal value of the shares issued but are also called upon at the same time to actually allow the "loss" thus arising on account of the supposed re-sale of the 3,79,439, 10 Rs. shares in the Burma Corporation (India) Ltd., to the promoter company which pretended to have sold them to it 4 years back.

13. So long as no part of the purchase consideration for the shares allotted was handed over to the Petitioner Company, we have to take it that all that the latter got for the shares issued by it was a promise to be given certain shares in exchange. Until the shares were actually handed over, we can hardly take it that the consideration was satisfied. The shares were never handed over. They were kept by the two promoter companies and utilised for their own pur-

poses until they were sold. The sale proceeds were not actually handed over to the Petitioner Company so that it might deal with them as it liked, but were kept as a deposit by the two promoter companies. But taking it that this deposit amounted to a payment, all that these extraordinary transactions establish is that for shares issued as fully paid up on 11th February 1920, no consideration was paid till January 1924 when credit for Rs. 2,62,76,628 was given for them though their face value was Rs. 3,12,81,600. In other words, though on 10th February 1920, the agreement was to hand over a Burma Corporation share of the then market value of Rs. 98-14/17 for each share allotted, nothing was done till January 1924 when cash credit was given at Rs. 168 per share issued. Upto January 1924, we had thus on the one side an actual issue of 1,56,408 shares with nothing on the other side except unfulfilled agreements to deliver certain shares. Disregarding these agreements, the whole transaction amounts to issuing in 1920, 1,56,408 shares of Rs. 200 each and receiving consideration for them in 1924 at the rate of Rs. 168 per share. Look at the matter in whatever way we like, it all amounts to issuing shares at a discount. In such circumstances, neither the Commissioner of Income-tax for taxation purposes, nor, I would respectfully submit, any Court of Justice in other proceedings, can be bound to accept as the price paid for the Burma Corporation shares, the nominal value of the shares allotted.

14. Now, my Lords, I proceed to consider the second question. The detailed analysis of the six agreements (Exs. A to F) in the preceding paragraphs shows that till the date of the actual sale of the Burma Corporation shares, they were not handed over to the Petitioner Company but kept by the two promoter companies with power to pledge them as security for their own liabilities. As the shares were not delivered, they did not even form part of the assets of the Petitioner Company which cannot in any sense be said to have been dealing in them. Before one can deal in anything, he must have it completely at his disposal. The shares were not at the disposal of the Petitioner Company but actually at the disposal of the two promoter companies which had power to pledge them as security for loans taken by them as stated above. The promoter companies were really all along dealing in them. The shares did not thus form part of the trading stock of the Petitioner Company. In its Balance Sheets (copies submitted herewith together with those of the Profit and Loss Account, Exs. M, N and O) for the years ended 31st March 1921, 1922 and 1923, these shares do not appear. What is shown regarding them is described as under in the first two Balance Sheets:—

“Investments:—

Interest in shares of the Burma Corporation Limited to be issued to this company in exchange for shares in this company already issued and to be issued in terms of the agreements with the Share Guarantee Trust Limited and the Intercontinental Trust (1913) Ltd., dated 10th February 1920..... Rs. 3,12,81,600.”

The entry in the Balance Sheet as at 31st March 1923 is peculiar since though it purports to record the state of affairs on 31st March 1923, it refers to the agreement dated 14th November 1923. It is as under:—

“Investments:—

Interest on 43,79,438 shares of the Burma Corporation Ltd., to be issued to this Company in exchange for shares in this company issued in terms of the

agreements with the Share Guarantee Trust Ltd., and the Intercontinental Trust (1913) Ltd., dated 10th February 1920 and supplemental agreements of 14th November 1923.....Rs. 3,12,81,600."

15. The above Balance Sheets make it clear that the Petitioner Company never had the Burma Corporation shares with it. What it had is described by it as "interest" in shares "to be delivered". The Petitioner Company has not trafficked in this "interest". What has been done is merely to convert the shares into cash before delivery so that instead of the shares, cash alone could be delivered. Article III (3) (Ex. P) of the Memorandum of Association is relied upon by the Petitioner Company to prove that it had the power to deal in these shares. This article is as under:—

"(3) To hold, improve, manage, exchange, mortgage, sell, dispose of, turn to account or otherwise deal with the said shares and (1) or stock and all other, if any, the property and rights of the company".

As, however, the shares were never delivered to it, it never held them nor improved them nor managed them nor in any way dealt in them as stock-in-trade as they were exchanged for cash before delivery to it.

16. The Petitioner Company relies upon the case of *Commissioner of Taxes v. The Melbourne Trust Co., Ltd.*, (1) and contends that the shares formed circulating capital. The facts of the present case are, however, entirely different from those in the above case. Therein the company concerned had with it the assets dealt with by it and it went on dealing in them. The assets were not at the disposal of some other companies; nor were they pledged or liable to be pledged as security for the business of others. There is nothing whatever in common between that case and the case of the Petitioner Company. The Burma Corporation shares not having been delivered at all could not and did not form part of its circulating capital. The 'interest' which the Petitioner Company had in them can at best be regarded as fixed capital only and nothing else.

17. In accordance with your Lordships' directions, the Petitioner Company was given a chance to put in additional evidence in this connection which is submitted herewith. It consists of the following:—

(1) Deposition of Mr. J. E. Sandeman, a director of the Petitioner Company (Ex. L*),

(2) The deposition of Mr. D. L. Stivens, Chartered Accountant, of the firm of Messrs. A. F. Ferguson & Co., (Ex. Q*).

(3) A copy of the Memorandum and Articles of Association of the Petitioner Company (Ex. R*).

(4) An agreement dated the 9th March 1920 between the Petitioner Company and one of the two promoter companies, viz., the Share Guarantee Trust Limited to take over certain other shares in exchange for 4,300 shares in the Petitioner Company to be allotted as fully paid (Ex. S*).

The point sought to be proved by tendering this evidence is that losses incurred in the years 1920-21, 1921-22 and 1922-23 by selling shares obtained

*Not printed.

(1) (1914) A.C. 1001.

from the Share Guarantee Trust Ltd., in exchange for the 4,300 shares in the Petitioner Company allotted under the agreement now put in (Ex. S) has been in the past allowed for income-tax purposes by the Senior Income-tax Officer. Hence, it is argued, the present loss must also be allowed. The inherent weakness of such an argument will be patent to your Lordships as even though the Income-tax Officer might have made a mistake in the past, he is not bound to repeat it. The real fact is that all these losses have *not* been allowed by the Income-tax Officer and tax has been actually levied and paid disregarding some of them as shown below. Also the agreement now put in (Ex. S) was never before shown to the Income-tax Office, nor was it informed that the shares sold were obtained in exchange for a capital issue. The Income-tax Office too never imagined such a possibility. Moreover, in the case of these shares, there was no agreement that delivery should be postponed and the shares should be kept with the promoter company concerned to be utilised by it for its business etc., as in the case of the Burma Corporation shares. Thus the case of these shares differs in this important respect from the Burma Corporation shares in dispute.

18. Now I proceed, my Lords, to state in brief how the above losses were dealt with in each of the above three years:—

(1) 1920-21 Profit and Loss Account (Ex. M*) :—

The receipts were only Rs. 2,872-1-4 and expenses Rs. 4,123 excluding totally "Depreciation and loss on sale of shares" claimed. The Company had to be exempted and there was no necessity to enquire into the nature of the share losses claimed as there was loss even after omitting them altogether.

(2) 1921-22 Profit and Loss Account (Ex. N*) :—

Rs. 1,575 were claimed as loss on realisation of the Burma Finance Shares and Rs. 600 on account of a motor car. The whole of this amount of Rs. 2,175 was disallowed as will be seen from the certified copy of the assessment order (Ex. T*) submitted herewith. The tax thus assessed was actually paid by the Petitioner Company on 14th February 1923 without protest.

(3) 1922-23 Profit and Loss account (Ex. O*) :—

'Depreciation on investments' amounting to Rs. 11,674 was claimed. This was disallowed at first. Later on Mr. D. L. Stivens, Chartered Accountant of Messrs. A. F. Ferguson & Co., himself appeared before the Senior Income-tax Officer and stated that the Petitioner Company valued its investments when accounts were closed and also was prepared to pay when appreciation took place on revaluation or sale. The Senior Income-tax Officer thereupon allowed this depreciation on investments. A true copy of the proceedings and the Senior Income-tax Officer's order accompanies (Ex. U*). This is the whole past history of the losses. It will be seen that in the first year, the question of loss on these investments did not arise at all. In the second year, the loss was actually disallowed without any protest on the part of the Petitioner Company and in the third year, depreciation on certain investments was allowed on the strength of Mr. Stivens' statements. I leave it to your Lordships to decide what help the Petitioner Company's case gets from these. To my mind, these profit and loss accounts and Mr. Stivens' statements prove for certain

that the "interest in the Burma Corporation shares to be delivered" was positively regarded by the Petitioner Company all along as fixed capital, whereas the other investments which were valued as stock-in-trade from year to year were treated as circulating capital. There is no stronger argument for this than the fact that the Burma Corporation shares were not valued at the end of each year as stock-in-trade, whereas the other investments were actually so valued each year and the profit or loss resulting was worked out and taken into account in the revenue account. Mr. Stivens definitely informed the Senior Income-tax Officer that the Petitioner Company did value its securities as stock-in-trade and charged depreciation or appreciation to the revenue account and was prepared to pay on the result of their sales too. Why were the Burma Corporation shares excluded from such valuations and from the revenue accounts all along upto the year in which they were sold? Simply because the "interest" therein was actually regarded by the Petitioner Company itself as fixed capital and not as stock-in-trade. All the authorities cited by the learned Chief Justice on this point have had my careful consideration and my confirmed opinion now on fully going through this question is that if it is to be taken that there is loss in the transaction, it is nothing but capital loss. This question was not exhaustively discussed previously as surmised by the learned Chief Justice in his judgment because the main point was and is that there could be no loss at all in a transaction of this nature.

19. Now turning to question 3, as repeatedly stated above, the Burma Corporation shares were never brought to India. They were kept in England and the sale proceeds retained in England. The whole transaction thus took place outside India. Now section 4 (1) and (2) of the Income-tax Act, 1922, runs as under:—

"4 (1) Save as hereinafter provided, this Act shall apply to all income, profits or gains as described or comprised in section 6, from whatever source derived, accruing or arising or received in British India, or deemed under the provisions of this Act to accrue or arise, or to be received in British India.

"(2) Profits and gains of a business accruing or arising without British India to a person resident in British India, shall, if they are received in or brought into British India, be deemed to have accrued or arisen in British India and to be profits and gains of the year in which they are so received or brought notwithstanding the fact that they did not so accrue or arise in that year, provided that they are so received or brought in within three years of the end of the year in which they accrued or arose.

"Explanation:—Profits or gains accruing or arising without British India shall not be deemed to be received or brought into British India within the meaning of this sub-section by reason only of the fact that they were taken into account in the balance sheet prepared in British India".

Under section 4 (1), the Indian Income-tax Act applies only to income, profits or gains accruing or arising or received in British India or deemed under the Act to so accrue or arise or to be received. The explanation to sub-sec. (2) distinctly lays down that profits or gains accruing outside British India to a resident of British India shall not be deemed to have been received or brought into British India simply because they are taken into account in the balance sheet

prepared in British India. The Act thus does not apply to transactions outside British India and the profit or loss resulting therefrom cannot be taken into account in levying tax in British India.

20. My opinion *re*: the third question therefore is that the alleged loss, if any, cannot be taken into account here as it relates to a transaction which has taken place wholly outside British India.

21. A copy of your Lordships' final judgment may kindly be certified to me as required by section 66 (5) of the Act for further action.

22. The original reference received with letter No. 6186 of 23rd November 1926 from the Registrar, High Court, is returned herewith. Two mistakes on its pages 1 and 11 have been duly corrected in red ink and initialled.

Bhulabhai J. Desai with *Messrs. Craigie, Elunt and Caroe*, for the Assesseees.

Taraporewala with the *Solicitor to Government*, for the Crown.

JUDGMENT.

MARTEN C. J.:—The assesseees, the Trustees Corporation (India) Limited, have been assessed to super-tax for the financial year ending the 31st March 1925 based on the income of the previous year ending the 31st March 1924. This is under sections 3 and 55 read with the definition of "previous year" in section 2 (11) of the Indian Income-tax Act, 1922. The main income on which they have been assessed is Rs. 18,43,148 representing the dividends paid by a Company which I will refer to as "The New Burma Company." The assesseees, however, say that against these dividends they have suffered a trading loss in respect of the acquisition and subsequent sale of the New Burma shares, and that they are entitled to set-off that loss against the dividends. For that purpose they say that the face value of their own shares which they paid to secure the Burma shares must be taken as the cost price and that in law it is not open to the Commissioner to take any other price than this face value. They further say that this loss is a trading loss, is opposed to a capital loss and moreover that it can be brought into account under section 4 of the Act, although the new Burma shares were sold in London and the proceeds have not yet been remitted to India.

The case came before us originally on the 5th October 1926 when after a partial hearing we remanded it back for additional evidence and otherwise for the reasons stated in our judgments of that date. The Commissioner made his further reference on the 12th March 1927, but unfortunately for various causes including the insufficient number of Judges to cope with the heavy work of this Court, my brother Kemp and I were not able to take up the case again until last month. As a result of that further reference the Commissioner has found certain further facts. But in the light of the full arguments we have now heard it would appear that important aspects of the case have not been dealt with in that reference. We have accordingly by consent admitted certain further evidence. The nature however of the transactions between the assessee Company, (whom I will refer to as "the Indian Company") and its two promoting Companies, the Share Guarantee Trust Limited and the Inter-Continental Trust (1923) Limited, (whom I will refer to as "the English Com-

panies"), are so peculiar that even after this full argument it is difficult to be sure that every possible way of regarding the problems presented to us has been exhausted.

I will now explain the reasons why I say this. We start with the fact that the two English Companies were undoubtedly the promoters of the Indian Company, and that they were also the vendors to it of a large block of shares in the Burma Corporation Limited, which I will call the Old Burma Company. That block of shares in the Old Burma Company amounted in all to 3,12,817 shares of £1 each. At the date of the original agreements between the English Companies and the Indian Company, these £1 shares in the Old Burma Company were standing on the London Stock Exchange at £14 per share. Therefore the apparent value of these Old Burma shares on the London market at that date was $312,817 \times 14 = \text{£ } 4,379,438$. Now at the then rate of exchange the market value in rupees of each Old Burma share worth £14 was Rs. 98-14/17.

It was under those circumstances that the first agreement, Exhibit A, of the 10th February 1920, and the contemporaneous agreement, Exhibit C, of the same date came to be executed between the Share Guarantee Trust Limited and the Indian Company. Similar agreements of the same date, Exhibit B and Exhibit D, were executed between the Inter-Continental Trust (1923) Limited and the Indian Company. Exhibits A and C on the one hand and Exhibits B and D on the other hand are in the same form. So nothing turns on that. It may, however, be borne in mind for purposes of identity that the parties are transposed in Exhibit C as compared with Exhibit A, and similarly in Exhibit D as compared with Exhibit B. Why it was thought expedient in each case to have two documents like Exhibits A and C instead of one does not appear, but such was the case. The effect of Exhibits A and D was that the English Companies agreed to sell to the Indian Company 134,705 and 178,112 shares making altogether the above block of 312,817 shares in the Old Burma Company. In payment the Indian Company was to allot to the English Companies the same number of shares in the Indian Company *viz.*, 312,817. But the face value of each share of the Indian Company was Rs. 200. Consequently stopping there the Indian Company was giving Rs. 200 a share, but only getting in return an Old Burma share then worth Rs. 98-14/17.

There was this further provision that in the event of the Old Burma shares being exchanged prior to completion for New Burma shares, then New Burma shares should be substituted for Old Burma shares at the rate of 14 new shares of Rs. 10 each for each old share of £1. That event in fact happened. But for the moment I will continue the story as to the Old Burma shares.

Next when one turns to Exhibit C, one finds provisions of a most extraordinary character. The Indian Company, so far as it was concerned, was to allot half of its own stipulated shares at once, and this in fact was done. Accordingly the English Companies thereby became the registered allottees and holders of the Indian Company's Share capital to the extent of half the stipulated number of shares. But on its part the English Companies were to be under no obligation to deliver the Burma shares for a space of three years except this that they were forthwith to deliver 25,000 Old Burma shares or their equi-

valent in New Burma shares. In fact the latter provision was never carried out. Nor in fact did the English Companies deliver any Burma shares at all even at the end of the three years period. Moreover under clause 3 they were to be at liberty to pledge the Burma shares for their own liabilities up to an aggregate of 2½ million sterling. In this respect it will be borne in mind that the then aggregate market value of the Burma shares was nearly 4-2/5 million sterling. Further, under clause 4 there was power for the English Companies to sell with the consent of the Indian Company and in that event the sale proceeds of the Burma shares were to be utilised in paying off the above liabilities of the English Companies to their own bankers and as to the balance in payment to the Indian Company, but in the former event the purchase consideration was to be reduced *pro tanto*.

The agreement does not specifically state whether, supposing no sale took place within the three years, the English Companies were to be at liberty to pay or set off any liability secured on these shares to their bankers as against their liability to deliver them to the Indian Company. It would certainly be a curious result if this important and extraordinary power was left to depend on the accident of whether there was an antecedent sale under clause 4 or not. But however that may be, it would seem clear that this sale to the Indian Company was not an absolute sale of the Burma shares, but was contingent to this extent *viz.*, on there being no pledge of these shares by the English Companies with their own bankers under clause 3, and no subsequent sale with the consent of the Indian Company under clause 4.

There followed in 1921 and 1922 two undertakings Exhibits V and VI given to the directors of the Indian Company, by which the English Companies undertook not to deal with the allotted shares of the Indian Company, and also were to indemnify the directors of the Indian Company in certain particulars.

When then the three years' period mentioned in Exhibit C expired in February 1923, the position appears to have been as follows according to the evidence before us. The English Companies had got half the stipulated shares of the Indian Company, but they had delivered none of the Burma shares, and on the other hand they had not pledged the Burma shares with their bankers, so we are told. Counsel for the Indian Company objected to the suggestion that the English Companies had at that date committed a breach of contract. Whether there was technically a breach of contract would depend on a full knowledge of the relations between the English Companies and the Indian Company which could probably only be obtained after full discovery in an appropriate law suit, to which the English Companies were made parties. But on the present material it can at any rate be said that while the Indian Company had done all that it was obliged to do up to that date, the English Companies on the other had failed to carry out their obligations. *Prima facie* therefore at that date the Indian Company was in a position to enforce delivery of the Burma shares, or alternatively to sue for damages. It would also seem that inasmuch as the English Companies had become the registered holders of this large block of shares in the Indian Company, and up to that time had given the Indian Company nothing for it except unfulfilled promises the legal result under the Companies Act would be that they would be liable as such registered

holders to pay up in full the nominal value of the shares of the Indian Company.

In fact, however, the Indian Company did not sue the English Companies but entered into two further agreements Exhibits E and F on the 14th November 1923. These agreements are made supplemental to Exhibits C and D respectively, and their effect is this. The English Companies are to deliver the Burma shares now represented by shares in the New Burma Company, but the date of delivery is extended to the 10th February 1926. That makes an extension of another three years from the expiry of the first three years fixed by Exhibit C. Then there is to be power for the English Companies to sell the New Burma shares with the consent of the Indian Company, but in that event the proceeds of sale are to be paid to the Indian Company together with all dividends received on them. There is another important provision *viz.*, that the original purchase consideration payable by the Indian Company is in effect to be reduced to one half. Consequently the shares of the Indian Company already allotted are to be taken as the whole purchase price payable by them, and on the other hand they are to receive the same amount of Burma shares that they originally agreed to buy.

Now that agreement does not state specifically whether the power of the English Companies to pledge the Burma shares with their bankers was meanwhile to remain in force or not. That point led to conflicting arguments before us, but it is at any rate clear that if a sale was effected under clause 2, then the whole proceeds were to go to the Indian Company, and were not to be applied in payment of any liability by the English Companies to their own bankers. So it may be said that here at any rate there is a firm contract for the sale and purchase of shares, which is no longer to be subject to the contingency of those shares being sold and the proceeds applied in discharge of the vendors' own liabilities. On the other hand the purchasers cannot count on delivery for another three years, though the vendors can deliver them as and when they like. And as the vendors had already got the whole purchase consideration in their hands, *viz.*, the shares of the Indian Company, it may be assumed that they would suit their own interests as to the time in which they would deliver the shares. In this respect there is also some doubt as to whether the undertakings given in Exhibits V and VI would continue after the date of Exhibit E. But that is a point we need not, I think, decide.

Another point of construction is of some importance. It arises with respect to the dividends. It is clear that if the Burma shares were sold before the 3 years with the consent of both parties, the dividends were to be paid to the Indian Company along with the proceeds of sale. But no express provision is made for the event of no such sale being effected prior to the expiration of the three years. It is consequently contended by counsel for the Indian Company that if the further three years had expired without any sale, then the Indian Company would not have been entitled to the interim dividends. In fact, however, a sale was effected under clause 2 of Exhibit E, *viz.*, in January 1924. The new Burma shares were then sold at London at 8s. per share, and this gives Rs. 168 as the sale proceeds of the Burma shares deliverable against each of the Indian Company's shares of Rs. 200 each.

I can now explain how the alleged loss arises. The Indian Company says that the cost price of the shares must be taken to be the 200 Rs. nominal value of each of its own allotted shares, and that on the other hand it only received in return Rs. 168, and consequently there is a loss of Rs. 32 per share which loss entirely wipes out the dividends received. Moreover they claim, as already indicated, that this loss is a trading loss.

Taking the questions submitted to us by the Commissioner, question 2 runs:—"Whether the alleged loss in question, if any, was capital loss or revenue loss." Now here it is clear that under its Memorandum of Association the Indian Company was formed to deal in shares and also to enter into the agreements of 1920 with the Indian Company above mentioned. Moreover the additional evidence now before us shows that it did have some dealings in shares of other Companies besides the Burma Company, and that over the years in question these dealings though limited in number were substantial in amount.

Under these circumstances, I think the case of the *Commissioner of Taxes v. The Melbourne Trust*, (1) is an authority to show that as the business of this Company was to buy and sell shares, the result of its share operations would be a trading profit or a trading loss as the case might be, and that consequently the losses as well as the profits in this respect could properly be brought into the profit and loss account. I appreciate the difficulty here that in fact the Indian Company never got actual possession of the Burma shares, but its various agreements from 1920 to 1924 in connection with these shares amounted, I think, to a trading in them. If then there was any loss over the Burma shares, I think it would be a revenue loss.

Turning next to Question 1, that asks us "whether the Commissioner of Income-tax was not bound in law to take as the price paid for the Burma Corporation shares the nominal value of the shares allotted by the petitioner Company in payment therefor." In my judgment that question must be answered in the negative on the facts of this particular case. I quite appreciate that in a normal case a company may be presumed to get an adequate *quid pro quo* for its own share capital which it allots as fully paid. But this is not necessarily so if after making all reasonable allowances for conflicting views as to values, there appears to be a substantial discrepancy between the value of the shares allotted, and the value of the article which the Company gets in return.

Thus in *In re Wragg Limited*, (2) at page 836, Lord Justice Smith says:—"Again, if in a registered contract a money value less than the face value of the share be placed upon the consideration which the Company had agreed to accept as representing in money's worth the nominal value of the share, that share, I should think, would not be fully paid-up; for instance, as was put in argument, a contract to supply to a limited Company 100 tons of coal, valued at 10s. per ton, as a consideration for 100 £1 shares in the Company—i.e., a value of £50 worth of coal for 100 £1 shares—these shares would not be, I think, fully paid-up."

According to the Crown, the proportion mentioned in that illustration is exactly the proportion in the present case. In the present case at the market

(1) (1914) A.C. 1001.

(2) (1897) 1 Ch. 796.

rates at the date of the agreements of 6th February 1920, the Indian Company was paying double the market value having regard to the then rate of exchange. No doubt the rate of exchange was then at almost the highest point, *viz.*, 2s. 10d. as compared with, say, 1|10 in August 1919, and 1|10 $\frac{1}{2}$ in September 1920 and 1|6-3|5 to 1|4 $\frac{3}{4}$ in December 1920. But on the other hand the English Companies sold at the highest price in the market, *viz.*, £ 14 per share, and as the income of the Burma Company was derived in rupees, *prima facie* the increase in the rate of exchange would also result in some increase in the sterling market quotations in London.

Counsel for the Indian Company has argued that in a transaction of this magnitude which amounted to the acquisition of approximately 1|3rd of the whole share capital of the Burma Company, one could not gauge the value of the shares in the same way as if one was buying a small quantity. On the other hand it is to be observed that this large block of shares came eventually to be sold in January 1924 and the then sale is agreed to have been effected at the then market price, *viz.*, 8s. On the evidence then before us I am quite unable to say that the fact that this sale was of so large a block as this would induce a purchaser to pay what ostensibly was double the then market value. Nor even allowing for optimism in a purchaser, am I prepared to say that he would regard the potential values of the Burma Company (which was a mining Company), to be so great that he was prepared to pay this apparently excessive sum. On the other hand I do recognise that presumably the amounts were fixed at some date prior to the 8th February 1920, for the agreements between the English Companies and the Indian Company could hardly have been negotiated, and prepared, and executed on the spur of the moment in Bombay. But in the absence of reliable evidence on this point, I am unable to attribute much importance to it. I would attach greater weight to the contention that neither party would be likely to negotiate on the basis of this 2s. 10d. rate of exchange remaining permanent.

After weighing then all the considerations, I think the difference here between the nominal value of the shares given and the market value of the assets purchased was sufficiently great as to entitle the Commissioner to challenge the adequacy of the consideration given by the English Companies.

But doing so, I come to the next point *viz.*, what is the proper method for ascertaining the cost price to the Company of these shares. The difficulty is caused by reason of Exhibit C and Exhibit D being what I have described as contingent contracts. Consequently one has to ask what price could one expect to obtain in February 1920 for shares which were not necessarily deliverable for 3 years, and perhaps not even then having regard to the powers of pledging retained by the vendors. On the whole I am inclined to think that the market value on the 10th February 1920 which the Commissioner has taken is the correct method. But even if it be held that the proper date to take is the date when all contingencies have ended, and when the Indian Company has a firm contract for the delivery to it of the Burma shares, then that date would be the 10th February 1923 when the first period of 3 years expired. The market price then, however, was substantially the same as in February 1920. It works out at about Rs. 92. Consequently there is no substantial difference in this respect whether one takes the market price at the beginning or at the end of the three years period. On that basis then it follows that on the figures before us there was in fact no trading loss by the Indian Company in respect of the

Burma shares, for the cost price was Rs. 98-14/17 in 1920 or about Rs. 92 in February 1923 and the sale price in January 1924 was about Rs. 168.

I should, however, deal with another aspect of the case which arose from a suggestion by the Bench and was afterwards the subject of lengthy arguments. Both counsel based their case on the values as at 10th February, 1920, but in the alternative, counsel for the Indian Company relied on the fact that the original contract was modified in November 1923 by Exhibit E with the result that eventually the Indian Company had only to pay half of what it originally agreed to do. Consequently it was said that substantially it got Rs. 200 in kind in return for its original share of Rs. 200, *viz.*, two Burma shares worth Rs. 98 each making Rs. 196 in all. Thereupon a question arose as to whether there was ever a firm contract between the parties until November 1923. In the result, as I have already indicated, I think there was, *viz.*, at any rate by the 10th February 1923 when the contingencies contemplated by Exhibit C had expired. Therefore I think by that date, if not earlier, the true cost price for the Indian Company had been ascertained. If, therefore, instead of enforcing the original contract as they might have done, they entered into new contracts which modified that cost price as part of a new bargain, then I think this was really a subsequent trading with the article originally purchased, and that it cannot truly be said that the contract in November 1923 represented the initial or true purchase price payable by the Company.

On that basis then it becomes unnecessary to decide what was the market value of the shares on the 14th November 1923 the date of Exhibits E and F. If, however, the 14th November 1923 be taken as the true date for ascertaining the cost price to the Company, then it is alleged by the Indian Company that the market rate on the 14th November 1923 as compared with the sale price in January 1924 would result in a heavy loss which would far exceed the amount of the dividends in question. This morning certain figures have been put in showing what was the market price on the 14th November 1923. They work out at 8s. 6d. to 9s. 3d. and inasmuch as the sale price in January 1924 is agreed to have been at 8s. it would follow that on that basis there would be a loss by the Indian Company which would exceed the dividends in question. This price on the 14th November 1923 was *ex* the first dividend of the Company declared in July 1923 and *cum* the second dividend declared in December 1923. So, too, the market price in January 1923 may be taken to have been *cum* the second dividend. On the other hand as between the English Companies and the Indian Company, the Indian Company received as a result of the sale in January 1924 8s. per share plus the first dividend, plus 5/6th of the second dividend declared in December 1923. One need not however, pursue these details, for some loss is shown. But as I have already said, I think the original contention of both parties that the correct date to take was the 10th February 1920 is the correct one, and that alternatively the 10th February 1923 should be taken and not the 14th November 1923.

In the result then I would hold that the assessment made by the Commissioner was made on methods which he was entitled to take in law. I say this because taking the Commissioner's figure of Rs. 98-16/17 as the initial cost price of the Burma shares to the Indian Company, which in law I think he was entitled to do, on the materials before us, there never was any real trading loss to the Indian Company. On that finding it becomes unnecessary to decide question

No. 3 as to whether any trading loss can be taken into account under section 4 in view of the fact that it is alleged by the Crown to have accrued and arisen outside British India.

I would only add that I have dealt with the case as above on the basis that the Indian Company and the English Companies were two independent bodies. In fact they were not, for it is clear that the Indian Company was under the control of its vendors and promoters the English Companies. But it is not the case for the Crown as presented to us that the contracts between the Indian Company and the English Companies were all paper transactions, and that the Burma shares in fact remained from first to last the property of the English Companies. No doubt the Commissioner has described the purchase consideration as fictitious. But that one understands having regard to the large discrepancy between the nominal contract price and the value of the article which the Indian Company got. It is not directed to show that these contracts were really benami for the English Companies, as was in effect the case in *Sir D. M. Petit v. Commissioner of Income-tax, Bombay* (1), where the law on the point is fully dealt with. Consequently I am unable to accept counsel's final argument to us for the Indian Company on the facts as found by the Commissioner that all the transactions are merely paper transactions, and consequently no duty is payable by the Indian Company as a separate entity.

I would accordingly answer the questions submitted to us as follows, *viz.*, Question 1, No. Question 2. The loss, if any, would have been a revenue loss but in fact there was no loss. Question 3. Unnecessary. I would direct the assessee, the Indian Company, to pay the costs including the costs of the first hearing in October 1926. Such costs to be taxed by the Taxing Master as on the Original Side scale.

KEMP J.:—This is a reference under section 66, cl. 3 of the Indian Income-tax Act XI of 1922

The circumstances giving rise to the reference are as follows:—In December 1919 a mining Company known as the Burma Corporation was registered in Rangoon. Of its £ 1 shares 1,34,705 were held by an English Company called the Share Guarantee Trust Limited and 1,78,112 by another English Company called the Inter-Continental Trust Limited. The total shares thus held by the two English Companies were 3,12,817 or nearly one-third of the whole share capital of the Burma Corporation. For brevity's sake I shall call the two Companies the English Companies. On 10th February 1920 the Burma Corporation shares were standing on the London market at £ 14. The rate of exchange was then 2s. 10d. and the equivalent in Rupees of the market price of the Burma Company's shares was Rs. 98.

On the same date, *i.e.*, 10th February 1920 the assessees whom I shall call the Indian Company were registered at Bombay under the Indian Companies Act 1913. The Indian Company was promoted by the two English Companies who were its sole proprietors with a nominal capital of 3,50,000 shares of the face value of Rs. 200 each. On that date by two similar agreements Exhibits A and B made one with each of the English Companies it was agreed that an equal number of the Indian Company's shares should be allotted for an equal

number of shares in the Burma Corporation. Clause 2 of the agreement contemplates the Burma Corporation being turned into a Rupee Company and in that event its £ 1 shares were to be exchanged for 14 years of Rs. 10 each, in the Rupee Company. By two similar supplementary agreements Exhibits C and D of the same date made one with each of the English Companies it was agreed that half of the Petitioning Company's shares forming the purchase should be allotted forthwith to the English Companies and the remaining half at the rate of one share in the Indian Company for two of the Burma Corporation shares or 28 shares of the Rupee Company. As to the Burma Corporation shares it was provided that 12,500 shares were to be delivered forthwith. As to the remainder they were to be delivered at the latest at the end of three years. In the meantime the English Companies were permitted to deposit or charge them as security to the Bank for any liability of the English Companies or other parties to the extent of £ 2,500,000. The supplementary agreements also provided that the English Companies could with the Indian Company's consent sell any of the undelivered shares and utilise the sale proceeds in discharge of the liability to the Bank in which event the purchase consideration was to be proportionately reduced or, if not so used, the sale proceeds were to be remitted to the Indian Company.

The effect of these agreements seems to me to be that there was an absolute undertaking by the English Companies to deliver the undelivered shares at the end of three years from the 10th February 1920 unless with the consent of the Indian Company they sold them at any time before the 10th of February 1923 in which case they were only bound to remit the sale proceeds, or balance of sale proceeds after discharging their liability to the Bank, to the Indian Company. It is clear, therefore, that if with the consent of the Indian Company all the undelivered shares were sold and the sale proceeds appropriated to the liabilities of the English Companies; the allotment of the Indian Company's shares would be limited to the 12,500 shares of the Indian Company allotted to such English Company. We are not concerned with how this abatement of the allotment was to be effected, once the Indian Company had allotted half the shares it is bound to allot under the agreement. It is equally clear that the sale of the remainder of the Burma Company's shares depended on the consent of the vendor companies and the effect of the agreements appears to have been that in any case there was no obligation on the English Companies to deliver the shares until after the lapse of three years from the 10th February 1920.

Here I may pause to state that before the Commissioner of Income-tax the Indian Company claimed that the face value of its shares should be accepted. The Commissioner being of opinion that those Rs. 200 shares merely represented the equivalent of Rs. 98 the price of the Burma shares standing at £ 12 in the English market when converted at the then rate of exchange 2s. 10d. held that that was the value to be taken for the Rs. 200 shares. As in the events that happened one question for us to answer is whether there was a loss sustained by the subsequent sale in England of the Burma shares it becomes a point of importance to ascertain at what value the Rs. 200 shares in the Indian Company should be taken. This much, however, is clear that the Indian Company had no control over the undelivered Burma shares except to assent to the English Companies selling them and that they were not entitled to demand delivery of the shares till the 10th of February 1923. I am of opinion that this

was a contract in effect for delivery, so far as the undelivered shares were concerned, of those shares three years from the date of the agreement and that the value of the Rs. 200 shares of the Indian Company cannot be ascertained by the value on the 10th February 1920 of a contract on such terms to deliver the shares three years thereafter. If no sale proceeds were remitted to the Indian Company the value of 25,000 of its shares at Rs. 200 each could fairly be taken at Rs. 98 the equivalent of a similar number of Burma shares at the rate of exchange then prevailing. In March 1923 the rate of the Burma shares appears to have been approximately 8s. 9d. which at the then current rate of exchange 1s. 4d. was equal to Rs. 6-9-0 a share. Therefore for 14 shares this would come to a little less than Rs. 92 which is even less than the rate of Rs. 98 on the 10th of February 1920. The rate in March 1923 may fairly be taken as the rate which prevailed in February 1923 when the undelivered shares of the Burma Company would become deliverable. I think, therefore, that the Commissioner could fairly under the agreement of the 10th February 1920 take the value of a Rs. 200 share in the Indian Company at Rs. 98.

It only remains to add that as a matter of fact the English Companies not only did not deliver 25,000 Burma Corporation shares to the Indian Company in pursuance of the agreement but they failed to deliver the remaining Burma shares at the expiration of three years from the 10th February 1920. Nor were the shares sold with the consent of the Indian Company. By two letters of indemnity (Exhibits V and VI) the English Companies undertook not to deal with the Indian Company's shares duly allotted to them. This was the state of affairs when on the 14th November 1923 two agreements Exhibits E and F described as supplementary agreements to those of the 10th February 1920 were made one with each of the English Companies. Exhibits E and F profess to modify and vary certain of the terms of the agreements of the 10th February 1920. The period of delivery is extended to the 14th November 1926 and in return for this concession the English Companies forego half the purchase consideration and agree to pay the Indian Company the proceeds of the shares should they be sold with the permission of the Indian Company at any time. Clauses 1, 2 and 4 of the principal agreement are said to be modified accordingly and no reference is made to clause 3 of the original agreement. In the view which I take of the construction of these agreements Exhibits E and F, clause 3 of the original agreement stood with the variation that the English Companies had the power to deposit or charge these shares for a further period of three years from the 14th November 1923. The original agreement was varied only so far as a further period for delivery was given of three years. The consideration in the Indian Company's shares was to be half the amount originally agreed upon to be allotted and the sale proceeds of the shares or any of them if sold with the Indian Company's consent were to be paid to the Indian Company and not to be appropriated to the discharge of any liability of the English Companies. Here again there was no obligation on the English Companies to deliver the Burma Company's shares until 14th November 1926 and only on that date unless there were a sale of the shares by mutual consent would the Indian Company have the complete control over the Burma Company's shares. As a matter of fact the power of sale was exercised with the Indian Company's consent in January 1924 and the shares were sold at 8s. The rate, therefore, at which these

Burma shares were sold was their value to the Company in return for half the number of the Petitioning Company's shares which it originally had to allot under the agreements Exhibits A and B. At 8s. and the rate of exchange of 1s. 4d. on that date the equivalent rate in India would be Rs. 6 or Rs. 84 for 14 shares, i.e., Rs. 168 for 28 shares equivalent to one share in the Petitioning Company of the nominal value of Rs. 200.

I am of opinion that the proper time to adopt for estimating the value of the Indian Company's Rs. 200 share was the time when the Indian Company actually acquired the right to complete control under the contracts (Exhibits A to D) of the Burma Corporation shares, i.e., 10—2—23. The value would be the market value of the Burmas in England at the then current rate of exchange or the sale price if they were sold. It is clear therefore that under no circumstances would the face value of Rs. 200 represent the actual value of these shares. I would therefore answer the first question in the negative and say that for the purposes of assessment the Commissioner was entitled to ascertain from the consideration paid in Burma shares for the Indian Company's shares the actual value of the Indian Company's shares. A difference of one shilling in the value of the Burma shares was equivalent at the exchange prevailing in January 1924 to a difference of Rs. 32,00,000. On the principle which I have adopted for valuing the Petitioning Company's Rs. 200 share there would be no loss sustained by the Petitioning Company by the resale of the Burma shares. As to the 2nd question referred to us by the Commissioner I am of opinion that as on 10th February 1923 the assessee acquired under the contracts Exhibit A to D the right to complete control over the Burma shares the subsequent contracts of 14th November 1923 were a dealing with the Burma shares within the business scope of the objects for which the Indian Company was formed. I therefore agree with respect with the answer given by the learned Chief Justice to question (2). I also agree with respect that question (1) should be answered in the negative. I see no necessity to return any reply to question (3).

[244] IN THE HIGH COURT OF JUDICATURE AT BOMBAY.

Before Sir Amberson Marten Kt., Chief Justice and Mr. Justice Kemp.

[13th March, 1928.]

The Bombay Trust Corporation Ltd., Bombay, as Agent
for the Hongkong Trust Corporation Ltd.

Assessee.*

v.

The Commissioner of Income-tax, Bombay

Referring Officer.

Income-tax Act (XI of 1922), Secs. 4, 40, 42 and 43—Loans by non-resident company to Bombay company—Interest remitted by Bombay company to non-resident company—Assessment thereon on Bombay company as "agent" of non-resident company—If legal—"Agent" liable only if in receipt of income—Non-resident company, if carrying on an assessable business in British India—Business connection—Statutory agents, when assessable.

* (1928) I.L.R. 52 Bom. 702; 30 Bom. L.R. 1172; A.I.R. (1928) Bom. 448.

Sections 40, 42 and 43 of the Income-tax Act should be read jointly and not disjunctively. The expressions "agent" and "income, profits or gains" in section 40 are extended by sections 43 and 42 respectively, but such 'agent' to be assessable must be in receipt on behalf of the non-resident of the income in question.

The word 'through' in section 43 does not mean from.

The H. T. Corporation, a financing company incorporated in Hongkong with a paid-up capital of 8 crores, during 1924 and 1925 lent deposits from time to time aggregating to 15 to 16 crores of rupees yearly to the assesseees, another financing corporation incorporated in Bombay with a nominal capital of 8 crores and a paid-up capital of a crore. These sums which were offered without security by the H. T. Corporation as fixed deposits at 5-1/4 per cent interest and accepted by the assesseees were remitted to Bombay through Messrs. E. D. Sassoon & Co., who through their offices at Shanghai and at Bombay acted as the intermediary banker for the remittance of the interest accruing on the deposits as well. The assesseees, who as "agent" of the H. T. Corporation were assessed on the sums of money payable as interest on the deposits, contended inter alia that no income accrued in Bombay and that in any event they were not liable to be assessed as "agent" of the H. T. Corporation. On a case stated under section 66 (2) of the Act.

Held, (1) that the assesseees, though "deemed to be an agent" of the H. T. Corporation under section 43 of the Act, could not be assessed as they were not in receipt of any income on behalf of the H. T. Corporation, the relation between the two companies being that of a borrower and a lender.

Imperial Tobacco Co. of India Ltd. v. Secretary of State, 1 I.T.C. 169, Followed.

(2) that the H. T. Corporation was carrying on an assessable business in British India with an income accruing or arising in British India within the meaning of section 4, either from "the business carried on" by it within the meaning of section 10, or from "other sources" under section 6 (vi) of the Act. *Smith & Co. v. Greenwood*, 8 Tax Cas. 193; *Grainger & Co. v. Gough*, 3 Tax Cas. 462; Distinguished.

(3) that there was a "business connection" between the assesseees and the H. T. Corporation within the meaning of section 43 of the Act.

Quære. Whether the H.T. Corporation can be assessed directly by sending a registered notice by post requiring them to make a return?

Obiter. The word 'property' in section 42 must be confined to the heading "property" in sections 6 (iii) and 9 and hence limited to immoveable property.

Case [Civil Reference No. 10 of 1927] stated under section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bombay for the opinion of the High Court.

CASE.

Under section 66(2) of the Indian Income-tax Act, XI of 1922 (India) (hereinafter referred to as the Act), and at the instance of the Bombay Trust Corporation Ltd., (hereinafter referred to as the assessee), I have the honour to submit for favour of your Lordships' opinion, certain questions of law

categorically set out in para 7 below *re*: the interpretation of sections 42 (1) and 43 of the Act, arising in connection with the assessments for the years 1925-26 and 1926-27 of the above Bombay Trust Corporation as agent of the Hongkong Trust Corporation.

2. *Facts of the Case.*—The Hongkong Trust Corporation is a limited company incorporated in Hongkong in July 1921. Exhibit A* is a copy of its Memorandum of Association and from it, it will be seen that it was established for the purpose *inter alia*, of (a) carrying on business as bankers and financiers, (b) advancing, depositing or lending money to or with companies and others and (c) doing this business at Hongkong or in *any part of the world*. [Article (3) (i), (ii), (ix), (xxvii), (xxxiii) and (xli).] The assessee *viz.*, the Bombay Trust Corporation Ltd., at whose instance this reference is being filed is a private limited company incorporated here in September 1920*. Exhibit B* is a copy of its Memorandum and Articles of Association and it shows that it too has power *inter alia*, to carry on business as capitalists and financiers, execute all kinds of financial operations, lend money to companies and others, carry on all kinds of agency business and “do all such other things as are incidental or conducive to the attainment of its objects.” [Article 3 (3), (8), (12) and (23).]

3. From the above, it will be seen that both these companies are banking and financing institutions. The paid up capital of the Hongkong Trust Corporation as stated by the assessee is 8 crores of rupees (*vide* please Exhibit F*). Besides this sum of money, it has at its disposal about 7 to 8 crores more on account of “total deposits received from all sources” as can be gathered from the statement put in by the assessee (Exhibit G*). Thus it had at its disposal in all about 15 to 16 crores of rupees and in virtue of its powers to do money-lending business in any part of the world, it appears to have confined its activities in this direction to Bombay where almost the whole of the above sum has been lent out from time to time in the shape of fixed deposits with the assessee at 5½ per cent interest.

4. Exhibit C* has been put in by the assessee to show how this money-lending business is being arranged and carried on. It is a copy of a telegram from the Hongkong Trust Corporation giving an extract from the minutes of the meeting of the Board of Directors of the Hongkong Trust Corporation held on 20—5—1924 and runs as under:—

“The Secretary was instructed to offer Bombay Trust Corporation Deposit for one year at 5½ per cent interest accrued to be remitted to Hongkong through E. D. Sassoon & Co., Ltd.”

From this, it appears that in accordance with it and other similar resolutions of the Board of Directors of the Hongkong Trust Corporation and in virtue of Article 3 (xli) of the Memorandum of Association authorising the Hongkong Trust Corporation to do business in any part of the world, offers must have been brought to Bombay from time to time to the Bombay Trust Corporation to receive deposits at 5½ per cent interest, these offers must have been accepted here and in virtue of them, various sums amounting at a time to several lakhs or a crore or two of rupees sent up here for being deposited with the assessee (*vide* please Exhibits D* & E*).

*Not printed.

5. The total amount deposited with the assessee throughout the calendar year 1924 was as much as 15 to 16 crores and the total interest paid thereon amounted to the exceedingly large sum of Rs. 88,22,544! For the calendar year 1925, it amounted to Rs. 82,44,115! Income-tax and super-tax on these sums was levied by the Senior Income-tax Officer for the year 1925-26 and 1926-27 respectively treating the assessee as the "agent" of the Hongkong Trust Corporation under section 43 of the Act. The total amount of income-tax and super-tax payable for these two years as per the assessments imposed by the Senior Income-tax Officer amounted to as much as Rs. 77,91,088-5-0.

6. Against the above assessments, the assessee appealed to the Assistant Commissioner stating *inter alia* that (a) the above income did not accrue here, (b) that even if it accrued here, the assessee could not be regarded as the "agent" of the Hongkong Trust Corporation, (c) that the whole of the amount paid as interest was not the income of the Hongkong Trust Corporation as it had to pay interest out of what it received to persons who had deposited money with it and (d) that as the Hongkong Trust Corporation was a company within the meaning of section 2 (6) of the Act, super-tax ought to have been levied at I anna in the rupee and not at the scale rates of 1 to 6 annas as was done by the Senior Income-tax Officer. As per the appellate order passed (Exhibit H*) the first two points were decided against the assessee and the last two in its favour. The result was that the total demand for the two years was reduced to Rs. 18,79,321-2-0. Not satisfied with this decision, the assessee has under section 66 (2) of the Act called for a reference *re*: the first two points taken up in appeal and decided against it for reasons given in its attorneys' letter No. 8054 of 2—5—1927 (Exhibit I*).

7. *Questions for the decision of the High Court*:—Your Lordships' opinion is respectfully required on the following questions of law as drafted by Messrs. Payne & Co., attorneys for the assessee. (*Vide* please Exhibit I*).—

(1) Whether the interest paid by the Bombay Trust Corporation Ltd., to the Hongkong Trust Corporation Ltd., on loans taken by the Bombay Trust Corporation Ltd., from the Hongkong Trust Corporation Ltd., is profits or gains accruing or arising to the Hongkong Trust Corporation Ltd., directly or indirectly through or from any business connection or property in British India;

(2) Whether such interest is liable to income-tax under the Indian Income-tax Act;

(3) Whether the Bombay Trust Corporation Ltd., can be treated as the Agent of the Hongkong Trust Corporation Ltd., for the purpose of section 42 of the Income-tax Act in respect of the interest so paid by the Bombay Trust Corporation Ltd., to the Hongkong Trust Corporation Ltd.;

(4) Whether the Bombay Trust Corporation can be deemed to be assessee under section 42 of the Act in respect of any income-tax which might be levied on the interest so paid by the Bombay Trust Corporation to the Hongkong Trust Corporation Ltd.;

(5) Whether the relation between the Bombay Trust Corporation Ltd., and the Hongkong Trust Corporation Ltd., was not purely that of a borrower

and lender and whether the Bombay Trust Corporation Ltd., as borrower could be deemed to be the agent of the lender the Hongkong Trust Corporation under sections 42 and 43 of the Income-tax Act in respect of interest payable on such loans and in respect of any income-tax that may be chargeable on such interest.

8. *Opinion of the Commissioner*:—As section 66 (2) of the Act requires me to give my opinion on the above questions while referring them to your Lordships, I beg respectfully to state as under after giving my best consideration to the arguments advanced in favour of the assessee as per its attorneys' letter of 2—5—1927 (Exhibit I).

9. Taking up questions (1) and (2), the section of the Act which has to be considered in this connection is section 42 (1). It runs as under:—

"42 (1). In the case of any person residing out of British India, all profits or gains accruing or arising to such person, whether directly or indirectly, through or from any business connection or property in British India, shall be deemed to be income accruing or arising within British India, and shall be chargeable to income-tax in the name of the agent of any such person, and such agent shall be deemed to be, for all the purposes of this Act, the assessee in respect of such income-tax:

"Provided that any arrears of tax may be recovered also in accordance with the provisions of this Act from any assets of the non-resident person which are, or may at any time come, within British India."

Now in this case, the fact that the Hongkong Trust Corporation is a non-resident person is admitted. That it is in receipt of a very large amount of interest on account of money lent here in British India is also undisputed. Under the above section 42 (1), we have to see whether this interest "accrues" or "arises" "directly or indirectly, through or from any business connection or property in British India". It is to be particularly noted that the section does not even require that the income should accrue or arise in British India as is supposed through stake by the assessee. All that it requires is that the income should accrue or arise *through or from any business connection or property in British India*. Hence we have to ascertain whether the interest income accrues or arises from a business connection here or from some property here.

10. Taking up "business connection" first, that the interest income accrues and arises from the money-lending business of the Hongkong Trust Corporation in Bombay is as clear as day light and hardly needs any proof. Fifteen to sixteen crores of rupees have been brought down to Bombay and lent out at interest and the interest income which the Hongkong Trust Corporation earns, accrues and arises directly from this money-lending business which is being carried on by it here for years together systematically ever since its incorporation. To see the exact nature of this money-lending business, we will go into some details about it here. Exhibit C shows how the deposits brought down here originate. The Board of Directors of the Hongkong Trust Corporation asks its Secretary to offer to the assessee certain sums as deposits at $5\frac{1}{4}$ per cent interest. These offers are then brought to Bombay to the assessee and are accepted and thereupon sums amounting at a time to lakhs and lakhs of rupees, if not crores, are brought down here and deposited with the assessee. Thus taking up the calendar year 1924, from Exhibit D which is a

copy of the account of the Hongkong Trust Corporation in the books of the assessee, it will be seen that on 1st January 1924, the latter had with the former, loans amounting in all to the gigantic sum of Rs. 16,17,32,885 as "fixed deposits" at $5\frac{1}{4}$ per cent interest. On 25th February 1924, a fresh deposit of Rs. 2 crores was received, on 19th, five deposits ranging from 1 lakh to 1 crore were repaid and Rs. 37,27,617 added to the balance outstanding on account of accrued interest. On June 21st, 15 deposits amounting in all to Rs. 4,70,26,265 were renewed. On July 19, Rs. 15,13,714 more were added for the same reason. On September 30th, a deposit of Rs. 10,17,807 was renewed. On November 29, six deposits amounting in all to Rs. 8,99,22,035 were renewed and so on. The total turn-over for the year was Rs. 33,72,23,534 and the total interest accrued thereon was Rs. 88,23,540! From Exhibits F and G, it will be seen that the total paid up capital of the Hongkong Trust Corporation was 8 crores and that it had besides about $7\frac{1}{2}$ to $8\frac{1}{2}$ crores of rupees on account of "deposits received from all sources." Thus it had at its disposal Rs. 15 to 16 crores which were all brought down here and deposited with the assessee. That a person who brings down here such large sums for the purpose of money-lending business here has a connection with British India is without any doubt and that connection can be nothing but a business connection, pure and simple. Can any one say that the Hongkong Trust Corporation has no connection whatever with British India? It has undoubtedly very intimate connection as all its capital and almost all the money deposited with it is kept by it here in Bombay in British India. It is kept solely for its business purposes—for the purpose of its money-lending business which under its Memorandum of Association (Exhibit A), it is empowered to do in any part of the world. Hence there is not the least doubt that the interest income accrues and arises from the business connection which the non-resident Hongkong Trust Corporation has with British India. This is quite enough to bring the income clearly and without any doubt within the four corners of section 42 (1) of the Act.

11. Not only does section 42 (1) apply to income accruing or arising from *business connection* in British India, but it applies also to income accruing or arising from "property in British India." Now the sixteen crores and odd of rupees which the Hongkong Trust Corporation kept here in British India as a fixed deposit is nothing but property in British India belonging to the non-resident Hongkong Trust Corporation. The word "property" in this section has its ordinary meaning including moveable as well as immoveable property. This property the Corporation keeps here with another Corporation to earn income thereby. A man may have house property or ready cash. As long as he keeps his property with himself, he can ordinarily earn nothing. It is only by parting with it for a time and allowing some one else to use it that income can accrue therefrom. As regards house property, it can be given in charge of another person for use by him for a fixed period in return for a fixed sum of money called rent. In the case of cash, it can be given in charge of another person for use by him for a fixed period in return for a fixed sum of money called interest. The two cases are exactly alike and I need hardly add anything further to justify an inference that the interest income accrues and arises to the non-resident Hongkong Trust Corporation on account of this property kept here in British India with the Bombay Trust Corporation.

12. For the above reasons, my Lords, my respectful submission as regards questions 1 and 2 which go together is that the interest income in question does undoubtedly accrue and arise from business connection as well as property in British India and so section 42 (1) does apply to this case without any doubt and that therefore the income is liable to tax.

13. The assessee contends that as this interest is payable to the Hongkong Trust Corporation at Hongkong as per Exhibit J*, it accrues and arises there and not in British India. As stated above, section 42 (1) does not require that the interest income should actually accrue and arise in British India. If it accrues and arises from a business connection or property here, it is to be deemed under this section 42 (1) to accrue and arise in British India and to be taxed. Hence the assessee's argument, even if it be correct, does not in the least prove its case. The income in this case as a matter of fact actually "accrues and arises" here in Bombay. These words "accrue" and "arise" are not defined in the Act, but Justice Mukerji in the referred case of *Rogers Pyatt Shellac Company v. Commissioner of Income-tax, Bengal* (1) has given a very lucid interpretation of these words which may safely be adopted. According to him, the word 'accrues' "connotes the idea of a growth or accumulation" and the word 'arises' "connotes the idea of the growth or accumulation with a tangible shape so as to be receivable." The word "accrues" he adds, means "growing or growing up by way of addition or increase or as an accession or advantage" and the word "arises" means "comes into existence or notice or presents itself." First of all, the income accrues and arises. As it were, it grows from day to day until it assumes a tangible shape so as to be receivable. The interest income in this particular case grows from day to day until it assumes the final shape when it can be received by the lender. From the day a deposit is brought down to Bombay and kept with the Bombay Trust Corporation, the interest income begins to accrue and arise. It goes on increasing from day to day until at the end of the fixed period of deposit, it assumes the final form when it becomes receivable and can be paid to the Hongkong Trust Corporation. It is thus clear that the interest income actually accrues and arises in British India and nowhere else, being the result of bringing down the money here and keeping it with the Bombay Trust Corporation. It would never have accrued or arisen, had the Hongkong Trust Corporation not brought down its money here but kept it with itself at Hongkong. The interest income accrues and arises here and when it assumes here a "tangible shape so as to be receivable," it is sent to Hongkong. If it actually accrued and arose at Hongkong as the assessee suggests, it could have been received there by the Hongkong Trust Corporation without being remitted from Bombay and there could have been no necessity to remit it from here through Messrs. E. D. Sassoon & Co., as is actually the case as stated by the assessee. My Lords not only does the income in question accrue and arise from a business connection and property in British India, but it actually accrues and arises in British India from these sources. The whole thing is so obvious that, but for the very large amount of tax involved, I would not have thought it desirable to trouble your Lordships to this extent.

*Not printed.

(1) 1 I.T.C. 363.

14. As the income in question accrues and arises from business connection and property in British India, under section 42 (1) it is to be deemed to accrue and arise within British India and must, under this very section, be charged to income-tax in the name of the "agent" of the non-resident and such agent is to be deemed to be the assessee in respect of such income-tax. This brings us on to questions (3), (4), and (5) and we have to see whether the assessee can be regarded as the "agent" of the Hongkong Trust Corporation for the purposes of section 42 (1). Now, my Lords, this word "agent" is not used in its ordinary sense in the Act in this connection but has a special meaning. Next to section 42 (1) is section 43 which defines what persons are to be treated as "agent" for the purposes of the former section 42 (1). It runs as under:—

"43. Any person employed by or on behalf of a person residing out of British India, or having any business connection with such person, or Agent to include persons treated as such. through whom such person is in the receipt of any income, profits or gains upon whom the Income-tax Officer has caused a notice to be served of his intention of treating him as the agent of the non-resident person shall, for all the purposes of this Act, be deemed to be such agent."

From this, your Lordships will see that the word "agent" has been, as stated above, given a certain special meaning and made to include "persons treated as such" including "any person having any business connection" with a non-resident, or "through whom such person is in the receipt of income, profits or gains."

The Senior Income-tax Officer having considered that the assessee had business connection with the Hongkong Trust Corporation and that the latter was in receipt of income "through" the former, served a notice on the former of his intention to treat it as the agent of the non-resident Hongkong Trust Corporation and after hearing it, treated it as "agent." On behalf of the assessee, it is contended that it cannot be treated as agent as it has no business connection with the Hongkong Trust Corporation and that the latter is not in receipt of any income through it.

15. We will first see whether the assessee has or has not any business connection with the Hongkong Trust Corporation. From what has been already stated in some of the preceding paras, my Lords, there appears to be no difficulty in arriving at a definite conclusion on this question. That there is a connection between the Bombay Trust Corporation and the Hongkong Trust Corporation goes without saying and is not disputed by any one. The only point is as to what sort of connection is that. In order to ascertain this, it is to be borne in mind that we are dealing with two limited companies formed for the very purpose of doing business as financiers, bankers, money-lenders etc., and connected together in the course of their business as such for a number of years to such an extent that one of them leaves with the other almost all or the major part of its resources amounting to 15 to 16 crores of rupees which the latter in turn invests in shares and securities paying to the former a princely income of over 80 lakhs of rupees per annum. In para 10 above are given details *re*: this connection between the two Corporations and hence they need not be repeated here again. Suffice it to say that all along, for the past several years, ever since the incorporation of the Hongkong Trust Cor-

poration, for the purposes of its business and business alone, the assessee takes as deposits the huge sums of money which the non-resident Corporation sends down here. It is in connection with the business and business alone of both these Corporations that the money-lending transactions from which the income taxed arises, take place and the connection thus brought about is nothing but a business connection. Even in their first petition of appeal to the Assistant Commissioner, the Solicitors for the assessee say that the Bombay Trust Corporation is formed principally "to invest moneys in shares and other investments for the purpose of gain" and that "*during the course of such business* the said Bombay Trust Corporation Ltd., took loans from the said Hongkong Trust Corporation and paid interest on such loans." If a connection thus arising between two admittedly banking and financing corporations is not "business connection," what else can it be? The words in section 43 are "*any business connection*" and my Lords, do not the circumstances of the case point to the assessee having a very close and intimate business connection with the Hongkong Trust Corporation? Is not the Bombay Trust Corporation connected with the Hongkong Trust Corporation in the course of its business and the business of the Hongkong Trust Corporation, on account of its business and the business of the Hongkong Trust Corporation and for the very purpose of its own and the business of the Hongkong Trust Corporation? Had they not been doing this banking and financing business, would this connection ever have arisen? Would they not have been perfect strangers to each other but for this connection arising out of their business? A connection which arises out of the assessee's business and which would not have been existent had it been not doing its business, is business connection and nothing else. The assessee says that the connection between it and the Hongkong Trust Corporation is that of a borrower and lender. For a connection to exist, however, there must be two or more parties to it between whom the connection arises, and by simply saying who the parties to a connection are, we do not define the connection itself. Husband and wife, father and son, borrower and lender, purchaser and seller etc., are all parties to certain connections existing between them and these are styled a "marriage connection" or "a family connection" or a "business connection" or whatever it might be. The connection between a borrower and a lender is itself a business connection arising out of money-lending business—at least in cases of the kind before us where Corporations borrowing and lending money to the extent of 16 crores of rupees for the purposes of the business for which they are incorporated, are concerned. If a Director of the Bombay Trust Corporation were a witness in a Court and were asked "Has your Corporation any business connection with the Hongkong Trust Corporation?", is it conceivable that he could reply "None whatever" without rendering himself liable to prosecution for perjury? The whole thing is so very clear and the wording of section 43 so very unambiguous that it is difficult to understand on what grounds the assessee can say that it is not liable. It is but just and fair that such a princely income earned here and here alone should pay tax as all other kinds of income earned here do and the person who is in charge of all the money belonging to the non-resident is certainly the person who should be called upon to pay on its behalf. This is most reasonable and one cannot for a moment imagine that the Income-tax Act was not meant for such cases.

In vain have I looked for any substantial argument in favour of the assessee. It is being alleged all along that the word 'agent'

is to be taken to have been used in its ordinary sense. In face of section 43, nothing would be more illegal and unjust than doing this in a case of this kind. In their letter of the 2nd instant (Exhibit I) giving the grounds for this reference, the assessee's Solicitors say that the bare fact that a non-resident does business with a resident and makes a profit out of such business does not constitute the resident the agent of the non-resident under sections 42 and 43 "and that these sections apply and were intended to apply only in cases in which the relation between the non-resident and resident is substantially that of Principal and Agent." When sections 42 and 43 do not at all, as a matter of fact, say any such thing and when their wording clearly applies to the present case, what is the use of saying that they are not meant for it? They are obviously meant for every case to which they apply. To support their view the assessee quotes what he calls "Rule 82 printed in the Income-tax Manual (1st Edition, pages 112-115)". The Government of India, have, my Lords, for the guidance of their officers issued an Income-tax Manual and therein given certain instructions to them. A "rule" made under the Act has, of course, the force of law but what the assessee calls "Rule 82" is not at all a rule but a para in the above Manual giving certain instructions to officers administering the Act. These instructions have no force of law and I know not whether your Lordships would even care to refer to them. However, in case your Lordships wish to have a look at them, I would respectfully point out that the assessee wants to rely on the instructions in para 84 (3), page 132 of the Income-tax Manual, 2nd Edition. These refer to the entirely different class of cases of "Indian agents of non-resident firms of which they are not technically either branches or subsidiary firms." The Government of India distinctly say that even casual agents in such cases are liable under the Act but that, for reasons with which I need not trouble your Lordships, in practice the liability be not enforced except in certain cases only. (*Vide* please section 60 of the Act empowering the Government of India to make an exemption, reduction in rate or other modification in respect of income-tax). Some illustrations are given below this para 84 (3) on which the assessee relies and I will not detain your Lordships long to prove that these illustrations have absolutely nothing to do with the present case. They refer to selling goods outright and have nothing to do with money-lending business. First of all, take the case of the Glasgow distiller referred to in illustration (a). What does he do? He *sells* to a trader here products of his distillery and does not *lend* them. Selling means parting with ownership and possession and lending means retaining one's ownership and this is what constitutes the chief difference between the case of the Glasgow distiller and the Hongkong Trust Corporation. The Hongkong Trust Corporation sells nothing to the assessee. It merely lends its money to it and I cannot see how the instructions *re*: the Glasgow distiller can apply to it. To make the fallacy in the arguments advanced clearer, I will take the case of a non-resident manufacturer of motor cars. If he sells his cars to a dealer here and parts with possession just as the Glasgow distiller does, his case will be on all fours with that case but if he merely gives his cars to a man here for being plied for hire as taxis, retaining his ownership, will the case be the same as that of the above distiller? Will it not be quite different then? What the motor car manufacturer will earn here in this way will be taxable and the person through whom he earns will be the agent without any doubt. The Hongkong Trust Corporation

sells nothing to the Bombay Trust Corporation as stated above. Purchasing goods is not the same thing as borrowing goods, - not to talk of borrowing money. One is a bit surprised when the assessee asserts that "there is no distinction between the seller and buyer of goods and the lender and borrower of money." The nature of the connection between the two is entirely different. One sells and parts with his ownership. The other does not. Moreover, the Government of India are actually of opinion that even the connection between the buyer and seller in the case of the Glasgow distiller and the belting manufacturer is such that section 43 does apply but that they do not want it to be so applied for certain reasons. It is because section 43 applies to such cases too that an executive order has had to be issued not to apply it in practice and it is really quite useless to rely on these instructions, which, if anything, entirely prove the case for the Crown.

16. The assessee further states that "if an Indian Company raises a Debenture loan in London and stipulates for payment of interest in London, the interest so paid is not liable to Indian Income-tax and need not be deducted at source" and that they "understand the Rule expressly provides to that effect." My Lords, in this connection I need hardly say that there is no Rule made under section 59 of the Income-tax Act which grants any such exemption as is alleged by the assessee. Also, the question is one of *deduction* of tax at source under section 18 (3) of the Act and not of a *regular assessment* under section 23 of the Act with which we are dealing in the present case. I cannot see how anything which relates to deduction of tax at source by the *payer* of interest can apply to a regular assessment of the *recipient* of interest. Deduction of tax at source is a duty laid on the person paying the interest. If that person be at London, our Income-tax Act cannot apply to him, but what has that to do with a regular assessment under section 23 read with sections 42 and 43 of the Act? Also going to London for a loan is quite different from having offers here in India to receive sums as fixed deposits as in the present case. The Bombay Trust Corporation did not go to Hongkong to raise loans there.

17. The assessee further alleges as under:—

"No doubt, the expression 'business connection' is extremely vague but it is submitted it implies that the non-resident has a connection with the resident under which the non-resident carries on business in British India through the resident."

The expression "business connection" can hardly be said to be vague though it is certainly very wide. It has a definite meaning and there is no chance of any one mistaking any other connection *e.g.*, a political connection or a family connection or a marriage connection, for a business connection. That is impossible. The expression is very wide especially as the words used are "any business connection" and not only "business connection." The connection between a non-resident and a resident through whom the former does business is only one particular kind of business connection and as long as section 43 does not confine itself to it alone and as long as it expressly uses the words "any business connection," it will be *prima facie* illegal to confine its meaning to any one particular class of business connection alone. Surely every one is perfectly aware of many other ways in which a business connection exists.

18. Your Lordships will easily perceive the reasons which impelled the Legislature to use the widest possible language in this connection. Non-residents have extra facilities to evade and avoid the tax on account of the fact of their being not resident in British India. To minimise the loss that would arise on their account special provisions have been put in the Act and the Rules as can be seen by a glance at sections 42 (1) and (2) and 43 and Rule 33. To make quite sure that no one might escape because of the want of a duly authorised representative in British India, any person having any business connection with a non-resident or through whom the latter is in receipt of any income, profits or gains is to be treated as the agent of the non-resident. What else could the Legislature do to equalise the burden of taxation on residents and non-residents and deal out equal treatment to all enjoying the benefits of the benign British rule?

19. The assessee further states that if tax is levied in such a case, every bank in India which receives a deposit from a non-resident will be liable to be assessed but that no one has even suggested that this be done. Whatever the law allows will be done, my Lords, be the person to be treated as "agent" under section 43 a bank or a company or anybody else. Everything depends on the merits of each particular case.

20. Not only does section 43 make a person having any "business connection" with a non-resident, the "agent" of the latter but it also lays down that a person "through whom" the non-resident "is in receipt of any income, profits or gains" is also to be regarded as his agent. The word "through" is wider than "from" and means "by means of" or "by the instrumentality of." (Webster's Dictionary). That the non-resident Hongkong Trust Corporation is in receipt of its interest income of over 80 lakhs of rupees by means of or by the instrumentality of the Bombay Trust Corporation is without any doubt. Without the instrumentality of the latter, it would never have earned this income.

21. For all the above reasons, my opinion is that the Bombay Trust Corporation has been rightly and justly treated as the agent of the Hongkong Trust Corporation within the meaning of section 43 of the Act and that even from the point of view of equity, nothing can be more justifiable than holding it to be the agent for this purpose as it and it alone can discharge the burden in the absence of the non-resident, being fully indemnified for the payment of the tax imposed under section 65 of the Act.

22. My answers to the five questions for the decision of the Hon'ble Court are therefore as under:—

(1) Yes.

(2) Yes.

(3) Yes.

(4) Yes.

(5) The Bombay Trust Corporation can be held to be the agent of the Hongkong Trust Corporation within the meaning and for the purposes of sections 42 and 43 of the Act.

23. A copy of your Lordships' opinion may kindly be certified to me for further action as required by section 66 (5) of the Act.

Bhulabhai J. Desai with Messrs. *Payne & Co.*, for the Assesseees.

Taraporewala with the *Government Solicitor*, for the Crown.

JUDGMENT.

MARTEN C. J.:—This income-tax reference arises on assessments for the financial years 1925-26 and 1926-27 of the Bombay Trust Corporation Limited (whom I will call "the Bombay Company") as agent of the Hongkong Trust Corporation Limited (whom I will call "the Hongkong Company"). Having regard to section 3 and the definition of "previous year" in section 2 (11) of the Indian Income-tax Act 1922, the profits assessed are alleged profits for the years ending the 31st March 1925 and the 31st March 1926 respectively.

The Crown claims that the Bombay Company has a "business connection" with the Hongkong Company and is accordingly the latter's agent within the meaning of section 43 of the Act, and can consequently be assessed in the name of that agent under section 42. The Bombay Company disputes the alleged "business connection," and says that in any event it is necessary, having regard to section 40 of the Act, for the alleged agent to be in receipt on behalf of the Hongkong Company of any income chargeable under the Act, and that consequently the Bombay Company is not liable, as sections 40, 42 and 43 must be read together and not disjunctively. Alternatively, they say that the Hongkong Company itself may be directly liable under section 4 of the Act, and that consequently an assessment ought not to be made on the Bombay company, more especially as the Bombay Company has no power of deduction under section 18 of the Act, and as section 19 provides that in other cases the tax should be paid by the assessee direct.

The material facts appear to be shortly as follows. The Bombay Company was incorporated in Bombay in September 1920. The Hongkong Company was incorporated in Hongkong in July 1921. The latter's Memorandum of Association Exhibit A shows that it was a financing Company as was also mainly the Bombay Company, as shown by its Memorandum Exhibit B. As regards their respective financial operations we have to deal with very large figures. It appears from para 3 of the case that the paid-up capital of the Hongkong Company was 8 crores of Rupees and that it had at its disposal about another 7 to 8 crores, thus making an aggregate sum of about 15 to 16 crores of rupees. The nominal capital of the Bombay Company was 8 crores, and we are told by counsel that their paid-up capital was one crore. Then in the years 1924-25 business took place between the two Companies on an enormous scale. It took the form of the Hongkong Company lending deposits to the Bombay Company at $5\frac{1}{4}$ per cent fixed interest. Those deposits amounted to about 15 to 16 crores in each of the years 1924 and 1925. Translating these figures into English currency, one finds that the Hongkong Company thus lent to the Bombay Company about 10 millions sterling per year. This was about double the nominal capital of the Bombay Company, and about 16 times its paid-up capital. Moreover such yearly advances were double the paid-up capital of the Hongkong Company and they also absorbed its remaining available deposits. The interest on these deposits amounted to over Rs. 88 lacs in 1924, and to over Rs. 82 lacs in 1925 payable by the Bombay Company. So far as appears from the papers before us, no security was taken for these huge deposits. The tax now claimed for the two years amounts itself to over Rs. 18 lacs.

The general terms of business are exemplified by the extract, Exhibit C, from the minutes of the Hongkong Company dated the 20th May 1924, *viz.*,

"The Secretary (Hongkong Company) was instructed to offer B.T.C. deposit (s) for one year at $5\frac{1}{4}$ per cent interest accrued to be remitted to Hongkong through E.D.S. & Co., Ltd." In this extract "B.T.C." stands for the Bombay Company and "E.D.S. & Co., Ltd.," stands for E.D. Sassoon & Co., Ltd., whom I will call "Sassoons." As to the *modus operandi* by which that interest is stated to have been remitted by the Bombay Company through Sassoons to the Hongkong Company, I may refer to Exhibit J for examples. There is first of all a letter of instructions from the Bombay Company to Sassoons of Bombay directing them to remit to the Shanghai house of Sassoons a sum of Rs. 2,625 and to "debit the same to our account." Secondly the Bombay Company writes to the Shanghai house of Sassoons as advising them of that remittance and asking them "to place it to the credit of the Hongkong Company at your end." Thirdly the Bombay Company writes to the Hongkong Company saying:—"We have advised Messrs. E.D. Sassoon & Co., Ltd., Shanghai to credit your account at their end with Rs. 2,625 being the interest on your deposit of Rs. 50,000 due to-day." These 3 letters are all dated the 6th September 1925.

We also had put in evidence a statement as to the reverse process, *viz.*, a letter of the 12th May 1926, from the Secretary of the Hongkong Company to the Bombay Company with reference to an original advance of money. It ran as follows:—"I am instructed to inquire whether or not you will agree to accept Rs. 1,25,00,000 (Rupees one crore and twenty five lacs) from us on call as from the 1st June next at $5\frac{1}{4}$ per cent annum interest. If you are prepared to accept this sum on the above-mentioned terms, instructions have been given to our Bombay Bankers—Messrs. E. D. Sassoon & Co., Ltd.—to pay you this amount, in exchange for which please send us your acknowledgment."

We were informed by counsel for the assessee that there was no written acceptance of this particular offer and that the acceptance was by conduct. There is, however, another letter of advice of the same date from the Hongkong Company to Sassoons of Shanghai in effect directing them to transfer Rupees $1\frac{1}{4}$ crores from the current account of the Hongkong Company with them to the Bombay house of Sassoons, and adding "Please advise your Bombay House that you hold this sum to their credit in rupees current account as on the 1st June 1926."

As regards the composition of these three companies, it is not suggested that any one of them is a mere creature of the other. But on the other hand, it is common ground that various members of the Sassoon family are interested in one or other of the three companies. Thus Capt. E. D. Sassoon is one of the signatories to the memorandum and one of the three first directors of the Bombay Company. Similarly Mr. H. W. Sassoon is one of the two signatories to the Memorandum of Association of the Hongkong Company. We were also told by counsel for the Bombay Company that the offices of the Bombay Company and of Sassoons are in the same building in Bombay.

Counsel for the Bombay Company submitted to us that in order to decide the five formal questions referred to us by the Commissioner, we ought to decide the following two questions, *viz.*, (1) Is the non-resident Hongkong Company carrying on an assessable business within British India, and (2) If so, can the present assessee, the Bombay Company, be sued in respect of

such non-resident? I think these two questions really involve the main points we have to decide and I will accordingly proceed to deal with them.

As regards the first question, in my judgment the Hongkong Company is carrying on an assessable business within British India. It is lending money regularly in British India from time to time, and is receiving interest in respect of such money-lending operations. It is to be noted that it sends its offers to Bombay which are accepted in Bombay. Its own moneys are paid in Bombay, and its interest thereon is earned in Bombay. Therefore, in my judgment, there is an income accruing or arising in British India within the meaning of section 4 either from "the business carried on" there by the Hongkong Company within the meaning of section 10, or else under another heading of section 6 *viz.*, sub-section (vi) "other sources."

The case then is very different from *Greenwood v. F. L. Smidth and Company Limited*, (1). There a Danish butter company was held not to carry on any trade in England, as all contracts and deliveries were made outside the United Kingdom. So, too, the present facts would seem to satisfy what Lord Herschell says in *Granger v. Gough*, (2).

"Does he, then, exercise his trade within the United Kingdom? It has been sometimes said that it is a question of fact whether a person so exercises his trade. In a sense this is true; but, in order to determine the question in any particular case, it is essential to form an idea of the elements which constitute the exercise of a trade within the meaning of the Act of Parliament. In the first place, I think there is a broad distinction between trading *with* a country and carrying on a trade *within* a country. Many merchants and manufacturers export their goods to all parts of the world, yet I do not suppose any one would dream of saying that they exercise or carry on their trade in every country in which their goods find customers."

But that again was a case where at most the foreign merchant canvassed for orders through agents in the United Kingdom, but all contracts for sale and all deliveries were made abroad. In saying this I appreciate the distinction pointed out in *Rogers Pyatt Shellac and Company v. Commissioner of Income-tax, Bengal*, (3) in commenting on *Board of Revenue v. Madras Export Company* (4) that the basis of this taxation is different in India from England. In India it is on income "accruing or arising or received in British India" or deemed so to be. (See *Board of Revenue v. Ramanadhan Chetty* (5)). In England it is mainly on a trade or business carried on there, supplemented (*inter alia*) by General Rules 5, 6 and 7 with reference to the agents of non-residents. But the first two cases I have cited are nevertheless useful on the limited point as to the meaning in section 10 of carrying on business.

Whether on my above finding the Hongkong Company could be assessed directly under sections 3 and 4 it is unnecessary to decide. The assesses here are the Bombay Company and not the Hongkong Company. But I may note in passing that under the recent decision of the House of Lords in *Whitney v. Commissioners of Inland Revenue*, (6) it has been held that a

(1) 8 Tax Cas. 193; (1922) 1 A.C. 417.

(2) 3 Tax Cas. 462; (1896) A.C. 325.

(3) 1 I.T.C. 363.

(4) 1 I.T.C. 194.

(5) 1 I.T.C. 37.

(6) 10 Tax Cas. 88; (1926) A.C. 37.

valid notice may be sent to a foreigner by registered post requiring him to make a return, and that on failure to do so he may be properly assessed by the Inland Revenue Commissioners under the English Income-tax Act. As to whether that decision would apply to our Indian Income-tax Act I say nothing.

I now turn to the second question, and this is the one which involves the real difficulty in the case. As to this, there are at least two competing views arising on the true operation of sections 40, 42 and 43. Are they to be read together, as was held with reference to these sections in the 1918 Act corresponding to sections 40 and 43 in the 1922 Act by the majority of Judges in the *Imperial Tobacco Company of India Limited v. The Secretary of State for India* (1), or are they to be read disjunctively, as was held in the dissenting judgment of Mr. Justice Ghose? The practical difficulty is this. All three sections deal with the agents of non-residents but section 40, the primary section, necessitates the agent in question "being in receipt on behalf of" the non-resident of the income sought to be charged. Section 42, however, makes no express reference to the agent being in receipt of the income.

We have heard full arguments on this point, and in the result I respectfully agree with the judgments of Mr. Justice Woodroffe and Mr. Justice Greaves so far as they are applicable, and would hold that these sections should be read jointly and not disjunctively. I will assume for the moment that any person who is deemed to be an agent within the meaning of section 43 is also an agent for the purposes of section 40. Stopping there, it is, I think clear that such agent, so far as section 40 is concerned, must be in receipt on behalf of the non-resident of the income in question. Then in the view which I take section 42 is directed to extending or explaining the profits of a non-resident mentioned in section 40, so as to make it clear that they include "all profits or gains accruing or arising to "the non-resident" whether directly or indirectly through or from any business connection or property in British India."

So, too, section 42 (2) contains certain provisions for assessing the profits of a non-resident foreign subject on a true basis where the Commissioner has reason to believe that owing to the course of business arranged between the resident and the non-resident, "the business done by the resident in pursuance of his connections with the non-resident produces to the resident either no profits or less than the ordinary profits which might be expected to arise in that business."

Next if one turns to section 43 there the word "agent" in section 40 is in effect extended to include "any person employed by or on behalf of a person residing out of British India, or having any business connection with such person, or through whom such person is in the receipt of any income, profits or gains," provided the Income-tax Officer has served on the resident a notice to that effect, and the resident has been given an opportunity of being heard as to his alleged liability. I may here notice that if these conditions are fulfilled, then the resident is to be deemed to be the agent of the non-resident "for all the purposes of this Act." Accordingly I think it clear that the word "agent" in section 40 will include what I may call this statutory agent in section 43.

My interpretation of the three sections will accordingly involve this that while in section 40 the term "agent" is extended by section 43, and "income, pro-

fits or gains" are extended by section 42. yet the condition that such agent should be "in receipt on behalf of" the non-resident of the income in question still remains. If on the other hand, a contrary construction be adopted, then one gets this result, that an ordinary and undisputed business agent cannot be made liable under section 40 unless he is in the receipt of income, but that on the other hand a statutory agent under section 43 is to be made liable under section 42 as an assessee, although he may not have any income on behalf of the non-resident.

This seems to me to be a startling conclusion to arrive at. It is one thing to make a man liable for a non-resident, if he is in the receipt of income on behalf of such non-resident. But it is quite another thing to make him liable if he has no such income out of which to pay the tax in question. In this connection I may draw attention to section 18 of the Act as regards deductions. The loans in the present case do not fall within that section. Consequently there is no power of deduction in the Bombay Company when it pays the interest due on the loans. On the contrary section 19 provides that in all cases other than those mentioned in section 18 "the tax shall be payable by the assessee direct."

The case then for the Crown, even when put at its highest, is I think one where in effect it is sought to impose a new liability on residents which did not previously exist, namely as statutory agents under sections 43 and 42 as opposed to agents in the ordinary meaning of that term, and that there is a serious doubt as to whether section 42 is intended to impose a personal liability on any alleged agent who is not in the receipt of income on behalf of the non-resident. Indeed, as I have already stated, the majority of the learned Judges in *Imperial Tobacco Co. v. Secretary of State of India*(1) have already held expressly that sections 31 and 34 in the 1918 Act corresponding to sections 40 and 43 in the present Act must be read jointly and consequently that receipt of income is necessary by a statutory agent under section 34. I should also infer that those learned Judges considered that the old section 33 corresponding to the present section 42 put the Crown in no better position. I appreciate that since the 1918 Act the words "or property" have been added to section 33 and the definition of "agent" in section 34 has been somewhat extended. But that does not, I think, affect the main ground of the decision which was that the agent in question must be in the receipt of income on behalf of the non-resident. I also appreciate that the specific questions then submitted to the Court had reference (i) to section 34 and (ii) to the propriety of the assessment generally. (See page 169). On the other hand in his dissenting judgment Mr. Justice Ghose says at p. 171: "Then comes section 33, subsection (1) of which has an important bearing on the present question." So it is clear that the effect of section 33 was fully before the Court. Indeed Mr. Justice Ghose held that section 34 ought to be read with section 33 rather than with section 31, and that as the receipt of income was not mentioned in section 33, the assessee was liable.

Under the above circumstances I am of opinion that the general principles referred to by Lord Buckmaster in *Greenwood v. F. L. Smidth*,(2) may fairly be called in aid. He says:—

(1) 1 I.T.C. 169.

(2) 8 Tax Cas. 193; (1922) 1 A.C. 417.

"It is, I think, important to remember the rule, which the Courts ought to obey, that, where it is desired to impose a new burden by way of taxation, it is essential that this intention should be stated in plain terms. The Courts cannot assent to the view that if a section in a taxing statute is of doubtful and ambiguous meaning, it is possible out of that ambiguity to extract a new and added obligation not formerly cast upon the tax-payer. Sub-section 2 here is at the best a sub-section of an extremely doubtful character....."

And if in the present case it be said that the construction which I would adopt would lead to some redundancy, the observations of Lord Sterndale in the same case in the Court of Appeal would seem to be in point. He says:—

".....And it would be very strange if another sub-section of the same section imposed an entirely new charge not within the schedule at all. I agree with Rowlatt J. that such a thing, if intended, should be carried out with the greatest clearness, and that if a reasonable meaning can be given to the sub-section without producing that effect such a meaning should be given....
.....Redundancy however is not unknown in legislation. I think it is better to impute such redundancy than to hold that such an important alteration has been made in the basis of taxation as the abolition of the condition of exercise of trade within the United Kingdom before a person not there resident can be taxed. To take the latter course would, I think, be to violate the well-known canon of construction of taxing Acts, that no one is to be taxed except by express words."

That then being my view of the construction of the Act, was the Bombay Company "in receipt on behalf of" the Hongkong Company of any income, profits or gains chargeable under the Act? In my opinion they were not. It is not suggested that they were agents in the ordinary sense of that word for the Hongkong Company. At most they were agents within the extended meaning given to that word by section 43. But in my judgment they never were in receipt of any interest on the loans on behalf of the Hongkong Company. On the contrary, it was their duty to pay that interest and not in any way to receive it. On the facts before us they had indeed no power to give a receipt, nor were they in any sense the trustees of the interest which was due from them.

So far then as I can see, the relations between them were that of debtor and creditor. As regards payment, for instance, the course of business as exemplified in Exhibit J. shows that the debtor in Bombay instructed his bankers in Bombay to debit his Bombay account and credit his Shanghai account with the amount requisite to pay the interest, and that then there followed a direction to the Shanghai branch of his Bombay bankers to credit that money in Shanghai to the Hongkong Company. This is mere payment of interest and nothing else. There is no receipt by the Bombay Company.

In his dissenting judgment in *Imperial Tobacco Co. of India Ltd. v. Secretary of State* (1) Mr. Justice Ghose states that "it would be to support an anomaly that a person receiving his income through an agent in this country would be assessed, but if he asks his debtor to remit the income

direct to him he would escape liability to pay the tax, a thing which this section was intended to remove." With all respect there seems to me a vast difference between the relations of mere debtor and creditor, and those of principal and agent. Nor am I prepared to concede that the Hongkong Company would necessarily escape assessment on my construction of the Act. On the contrary, as I have already pointed out, it may be that they could be assessed directly under sections 3 and 4 after notice served on them by registered post.

I may here mention one further argument by counsel for the Bombay Company. He said that on the hypothesis that the Hongkong Company were carrying on business within British India and earning profits there on that business, they would be directly liable under section 4, and consequently it would be unnecessary to invoke section 42, for the income thereby earned would be the income actually arising and not income "deemed to arise" within British India. Consequently he argued that if once you found the principal directly liable, you could not also fix an alleged agent with the same liability. It is unnecessary to decide that point because, as I have already indicated, my decision on the true construction of sections 40 and 42 is in his favour. But as at present advised I am disposed to think that in the case of a non-resident the Crown may pursue whichever remedy they prefer. I would accordingly respectfully agree with the decision of Sir John Wallis to that effect in *Chief Commissioner of Income-tax, Madras v. Bhanjee Ramjee & Co.*, (1) which was cited to us in the *Remington Typewriter case* heard next after this one. I of course appreciate that sections 3 and 4 are the main charging sections. On the other hand to determine what income is to be charged in certain cases one has to turn to sections 40 and 43.

So, too, my above finding on the true construction of sections 40 and 42 renders it unnecessary for me to determine whether there was a "business connection" between the Hongkong Company and the Bombay Company within the meaning of section 43. Or whether within the meaning of that section the Bombay Company was a person "through whom" the Hongkong Company was in receipt of the income. For the purposes of my main decision, I have been content to assume that the Hongkong Company is to be deemed to be an agent within the meaning of section 43. But as full arguments were addressed to us on the point, I may state that on the facts of the present case I would hold that the Bombay Company had a business connection with the Hongkong Company. I do not propose to define the words "business connection" as used in sections 42 and 43. For the purposes of the present case it is unnecessary to do so. On the other hand I am not prepared to accede to the argument presented to us by counsel for the Bombay Company to the effect that you must confine the expression "business connection" to a connection in the business of a resident person which gives rise to a pecuniary interest in the assets of that business, as *e.g.*, a share in the profits. But the facts here are most exceptional. We are dealing in enormous figures, and substantially the Bombay Company was being financed to the extent of 15 or 16 times its paid up capital by a fairy god mother in the shape of the Hongkong Company who was prepared to lend them almost unlimited sums at $5\frac{1}{4}$ per cent interest without security, and in its turn the Hongkong Company was risking double the amount of its paid-up capital and all its available deposits.

(1) 1 I.T.C. 147.

Under those circumstances it seems to me that there was a strong business connection between the two Companies. The business interests of the Hongkong Company were practically entirely wound up in the business welfare of the Bombay Company. The failure of the latter would have involved the ruin of the former. Consequently I need say nothing as to the fact that behind these strong financial ties there was the family house of E. D. Sassoon & Company Limited as the banker intermediary. Nor need I in any way lay stress on such family connections as there might be between the various share-holders or directors of the three Companies. The case can be decided quite apart from that, and I have dealt with it on that basis.

As regards the further question as to whether in any event the Bombay Company was a person through whom the Hongkong Company was in the receipt of income, I am inclined to think that the word "through" should not be construed as meaning "from". In other words, I do not think that that section was intended to include any person who might have to transmit moneys to a non-resident, whether or no he knew that such moneys represented the income, profits or gains of the non-resident.

I may add that as regards the decision in *Imperial Tobacco Co., of India Ltd. v. Secretary of State* (1) to the effect that the agent charged must be in receipt of income, there has been no subsequent alteration made in sections 40 to 43 on that point apart from the addition of the words "or property" in section 42 and the alteration I have already referred to in section 43. But on the other hand sections 57 and 58 have been amended so as to necessitate the deduction of super-tax as well as income-tax on dividends. That however is another point. Up to now the Legislature has not altered the general construction which the majority of the Judges in *Imperial Tobacco Co. of India Ltd. v. Secretary of State* (1) placed on sections 31 and 34 of the 1918 Act. It has met the finding in that case that the Company was not in receipt of its dividends on behalf of its shareholders, and consequently not within section 31, by extending the section for compulsory deduction of tax from such dividends.

As regards the meaning of the word 'property' in section 42, I think there is much force in the contention of the counsel for the Bombay Company that it must be confined to the heading property in section 6 (iii) and 9, and would therefore be limited to immovable property. But this point also it is unnecessary to decide in the present case.

In the result, then, I would answer the questions submitted to us as follows:—

1. Yes, from a business connection. But it also arises directly under section 4 (1) and section 6 (iv) or (vi).

2. Yes.

3 & 4. No, because the Bombay Company is not in receipt of any such interest on behalf of the Hongkong Company as required by section 40.

5. The relation between the two Companies was that of borrower and lender, but having regard to section 43 the Bombay Company though deemed to be an agent of the Hongkong Company for the purposes of sections 40 and 42 should not be assessed as they were not in receipt of income. (See answer to questions 3 and 4).

As regards costs, I would direct the costs of the Bombay Company to be paid by the Commissioner, such costs to be taxed by the Taxing Master, Original Side, as on the Original Side scale.

KEMP J:—The main question for our consideration in this reference is whether a Corporation called the Bombay Trust Corporation carrying on business in Bombay is properly assessed under sections 42 (1) and 43 of the Income-tax Act (XI of 1922) as the agent of another Corporation called the Hongkong Trust Corporation carrying on business in Hongkong in respect of the income alleged to accrue to the latter in Bombay. The facts giving rise to this reference are as follows. The Bombay Trust Corporation was registered in Bombay on 8th September 1920; the Hongkong Trust Corporation was registered at Hongkong on 6th July 1921. The paid-up capital of the Hongkong Trust Corporation amounted to 8 crores of rupees and it had at its disposal about 7 or 8 crores more of cash deposits received from all sources. It was formed as a limited company and by its Memorandum of Association it was empowered to carry on the business of bankers and financiers, advancing, depositing or lending money and doing this business at Hongkong or in any part of the world. In fact its activities were confined to Bombay and to lending money to the Bombay Trust Corporation. The Bombay Trust Corporation was a private limited company and by its Memorandum and Articles of Association its objects are stated *inter alia*, to be to carry on business as capitalists and financiers, lending money and executing all kinds of financial operations. There was undoubtedly an intimate connection between the Bombay Trust Corporation and the Hongkong Trust Corporation. The Hongkong Trust Corporation, as I have said, practically confined all its activities to its money lending business with the Bombay Trust Corporation in Bombay and lent the whole of the 15 or 16 crores constituting its paid-up capital and cash deposits to the Bombay Trust Corporation from time to time at $5\frac{1}{4}$ per cent interest. The interest accruing due was remitted by the Bombay Trust Corporation through its Bankers Messrs. E. D. Sassoon & Company, Bombay, to the Shanghai branch of the same bankers which kept an account of the Hongkong Trust Corporation. On the profits and income accruing to the Hongkong Trust Corporation from this money lending business for the years ending 31st March 1925 and 31st March 1926 the Commissioner has assessed the Bombay Trust Corporation under sections 42 (1) and 43 of the Indian Income-tax Act XI of 1922 as agent of the Hongkong Trust Corporation to income-tax and super-tax for the financial years 1925-26 and 1926-27.

The amount involved is large, the income-tax for 1925-26 amounting to Rs. 4,92,821 and super-tax Rs. 3,92,096, and for 1926-27 income-tax Rs. 5,38,510 and super-tax Rs. 3,55,882. The total, therefore, for the two years amounts to Rs. 18,79,321. At the request of the assessee the Commissioner referred certain questions for our opinion under section 66 (2) of the Indian Income-tax Act XI of 1922. Those questions are stated in paragraph 7 of the Commissioner's reference. He was of opinion that the interest received by the Hongkong Trust Corporation were profits or gains accruing through a business connection or property in British India under section 42 (1) of the Act and he was further of opinion that the Bombay Trust Corporation could be treated as the agent of the Hongkong Trust Corporation under sections 42 (1) and 43 in respect of such interest.

The first point for consideration is whether the income or profit accruing to the Hongkong Trust Corporation arose from a business carried on by it in Bombay and it seems to me clear that it did. The correspondence shows that the procedure adopted in lending these moneys was for the Hongkong Trust Corporation to make an offer from Hongkong to the Bombay Trust Corporation in Bombay to lend a sum of money. The Bombay Trust Corporation accepted the offer in Bombay and the contract, therefore, was made in Bombay. The business between the two companies formed a series of contracts from time to time and thus the whole of this money lending business was done in Bombay and the interest accrued here although it was remitted through Messrs. E. D. Sassoon & Company on behalf of the Bombay Trust Corporation to China. I think it is clear this business was done in Bombay and that the income from it accrued to the Hongkong Corporation in Bombay.

Another question however arises in considering what meaning is to be given to the words 'business connection' in sections 42 (1) and 43. The Sassoon family were interested very largely in both the Bombay and the Hongkong Trust Corporations as well as in the firm of E. D. Sassoon & Company whose Bombay Office is in the same building as the Bombay Company, through whom the moneys and the interest were remitted from time to time. There can be little doubt that although the Hongkong Trust Corporation and the Bombay Trust Corporation were separate legal entities, there was that intimate connection between them as shown by their dealings which shows that the Hongkong Trust Corporation was formed practically for the purpose of lending all its available cash to the Bombay Trust Corporation and the intermediary between the two Corporations were the bankers E. D. Sassoon and Company. The Hongkong Corporation lent all its paid-up capital and cash deposits apparently without security to the Bombay Company. Such a connection between the Hongkong Trust Corporation and the Bombay Trust Corporation would, I think, generally be regarded as a "business connection" and therefore the interest paid by the Bombay Trust Corporation was profits or gains accruing to the Hongkong Trust Corporation in British India. In this view of the question if the decision in *Whitney v. Commissioners of Inland Revenue* (1) is applicable to our Act the Hongkong Trust Corporation itself can be reached by a notice to make a return and be assessed on failure to do so in respect of this business done by it in Bombay.

But the further question arises whether the Bombay Trust Corporation are the proper persons who can be assessed as the agents, under sections 42 (1) and 43, of the Hongkong Trust Corporation. In *Imperial Tobacco Co., v. Secretary of State*, (2) the majority of the Court (Woodroffe J., and Greaves J.) held that sections 41 and 43 were to be read together and that therefore the statutory agent created by section 43 must be one who is in receipt of the income etc., on behalf of the non-resident. That case was decided in January 1922 prior to the coming into force of the present Act in March 1922. The present Act has added the words in section 43 "or through whom such person is in the receipt of any income, profits or gains," and it is to be noted, as the learned Chief Justice has pointed out, that the Legislature, had it

(1) 10 Tax Cas. 88; (1926) A.C. 37.

(1) 1 I.T.C. 169.

wished to disagree with the decision in *Imperial Tobacco Co. Ltd. v. Secretary of State* (1) had the opportunity in the present Act of clearly indicating that section 43 was not intended to be read with section 41 as extending the meaning of the word 'agent' only. On the other hand Act XI of 1922 was probably introduced prior to January 1922 and it is of course quite possible that the decision in *Imperial Tobacco Co. Ltd. v. Secretary of State* (1) was not then brought to the notice of the framers of the present Act.

Now as to the case of non-residents we have sections 40 to 43 of the Act. Section 40 says tax shall be levied and recovered from his agent who is in receipt on his behalf of any income, profits or gains chargeable under the Act. Section 4 (1) applies the Act to all income, profits and gains accruing or arising in British India. Also by it the Act may lay down that other income, profits and gains shall be regarded as accruing or arising in British India.

Here the profits or gains clearly accrued in British India and are therefore taxable. But assurance is made doubly sure by section 42 (1) which states that profits or gains accruing or arising to the non-resident from a business connection in British India shall be deemed to be income accruing or arising in British India and here I have held there is such a business connection.

Can it be successfully contended that in respect of income coming under both the descriptions of accruing in British India and deemed to accrue in British India under section 4 the agent liable to assessment for such income was intended to be vested with a different authority? I think not. I think that 'agent' in section 42 (1) must mean agent in receipt of income on behalf of the non-resident as in section 40. The income in section 40 includes the income in section 42 (1). Otherwise we have a contradiction as to the agent to be assessed.

Then section 43 creates a statutory agent. It does not substitute such agent for an agent in receipt of income on the non-resident's behalf. It says certain persons may be agents. They are:—

- (1) an employee,
- (2) one having a business connection with the non-resident and
- (3) One through whom the non-resident receives the income or, it may be, one whose possession of the income is the constructive possession of the non-resident. Neither construction of (3) matters here because the Bombay Trust Corporation are mere debtors and cannot in my opinion be regarded as fulfilling either description. If the Legislature had intended that the statutory agent should be the source of the income it should have said so in clear and unmistakable terms.

Nor is the business connection here existing between the two Corporations such that the Bombay Trust Corporation can be regarded as a person in receipt of the income on the Hongkong Trust Corporation's behalf.

Any other construction of section 43 would enable the Commissioner to serve any employee, who might not be in receipt of the income on the non-

resident's behalf, so as to constitute him an assessee under the Act. This would be inequitable and can hardly have been intended and at any rate any such liability should be expressed in clear and unambiguous terms. Having regard to the loose drafting of sections 40, 42 (1) and 43, I decline to hold it has this effect.

Further, I agree with respect with what the Chief Justice has pointed out in his judgment which I have had the advantage of perusing. If in this case there is no power of deduction under the Act the tax is payable by the assessee direct.

I agree with respect with the Chief Justice as to the answers to the questions submitted for our opinion.

[245] IN THE HIGH COURT OF JUDICATURE AT PATNA.

Before Sir Dawson Miller Kt., Chief Justice and Mr. Justice Koss.

[14th March, 1928.]

Maharajadhiraj of Darbhanga

.. Assessee*

v.

The Commissioner of Income-tax, Bihar and Orissa .. Referring Officer.

Income-tax Act (XI of 1922), Secs. 2 (1) (a), (c), and 4 (3) (viii)—Nazar paid for recognition of transfer of non-transferable holdings—Landlord's fees—If exempt from assessment as agricultural income—Building contiguous to Zamindar's dwelling house used as guest house—Claim of exemption from assessment, proper test for determination of.

Nazar or Salami paid by the raiyats to the landlord in consideration of the latter recognising the transfer of a non-transferable holding and the fees, known as landlord's fees, realised by the landlord under section 12 of the Bengal Tenancy Act are agricultural income within the meaning of section 2 (1) (a) of the Income-tax Act and as such exempt from assessment under section 4 (3) (viii) of the Act.

Mehr Bano Khanum v. Commissioner of Income-tax, Bengal 2 I.T.C. 99, Followed.

The assessee, the Maharajah of Dharbhanga, claimed exemption from assessment to income-tax in respect of a building situate in the same compound as his principal dwelling-house in Dharbhanga and used principally as a guest-house for European guests. The claim was disallowed on the ground that having regard to the fact that the assessee's income was not derived exclusively from land but also from other sources such as business in stocks and shares, the guest-house was not required by him as a zamindar but as a person of great wealth and social position. On a case stated to the High Court under section 66 (3) of the Act in compliance with the order of the High Court,

Held, that it not being disputed that the assessee required a dwelling house in that locality by reason of his connection with land, he was entitled to

the exemption under section 2 (1) (c) of the Act read with section 4 (3) (viii) and it was not open to the Commissioner judging by a standard set up by himself to consider whether the particular class of house was more or less than the actual requirements of the assessee as a zamindar.

It was immaterial for the purpose of claiming the exemption whether the building was really a part of the main dwelling-house itself or structurally unconnected with it.

Case [Miscellaneous Judicial Case No. 47 of 1926] stated under section 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bihar and Orissa, in compliance with the order of the High Court dated the 9th April, 1926.

CASE.

As directed by the High Court, Patna, in their order under section 66 (3) of the Indian Income-tax Act, in Misc. Judicial Case No. 47 of 1926, dated the 9th April 1926, I submit the following two points for decision of the Court.

(1) Whether the annual value of the building standing in the compound of the assessee (Maharajadhiraj of Darbhanga) ordinarily known as Chatra Bhawan is chargeable to income-tax, or, whether, on the other hand, it is exempted under the provisions of section 2 (1) (c) read with section 4 (3) (viii) of the Act.

(2) Whether *Nazar* or *Salami* paid by the raiyats to the landlord in consideration of latter's recognising the transfer of a holding which is not legally transferable or the legality of the transfer of which is doubtful, is agricultural income and is accordingly exempt from tax by virtue of the provisions of section 2 (1) (a) read with section 4 (3) (viii) of the Act and similarly whether landlords' fees realized by the landlord under the provisions of section 12 of the B. T. Act are agricultural income and accordingly not chargeable to tax.

2. The Chatra Bhawan is one of 3 blocks of building standing in a compound in Dharbhanga, the other two buildings in this compound being the Moti Mahal and the Anandbagh palace, the latter being used at the present time as the central zamindari office, while in a compound west of this and across a public road lies the palace proper ordinarily occupied by the assessee, his private office in a separate block, and the palaces of two Dowager Maharanis.

3. There is nothing on record to show when the Chatra Bhawan was built or for what object it was built, but it is not denied that it was at one time occupied as a school house by the sons of the assessee and the very name would appear to suggest that this was the object for which it was built, Chatra Bhawan meaning, I am told, "the abode of the students". On the other hand, it has been explained by an agent of the assessee that this building is so called after one Chatra Singh, an ancestor of the assessee.

4. The building is expensively furnished in European style and has been used for the accommodation of European guests of high rank and this would appear to be the purpose to which it is ordinarily put at present, the result being that frequently the building lies vacant for considerable periods.

5. If the valuation of the building in question is to be exempted from income-tax, the following conditions must be fulfilled:

(1) It must be owned and occupied by the receiver of the rent or revenue of agricultural land.

(2) It must be on or in the vicinity of such land.

(3) It must be a building which the receiver of the rent by reason of his connection with the land requires as a dwelling house or as a store house or other out-building. (Sec. 2 (1) (c) of the Act).

6. It is not denied that this building is owned and occupied by the assessee who is a receiver of rent, but it is the contention of the Department that it is not occupied by him *qua* receiver of rent as is explained below in paragraphs 8 and 9.

7. The next question is whether the building is on or in the immediate vicinity of the land, the rent of which he receives. In this connection, it is reported by the Income-tax Officer who has been specially asked to report on this point that though the assessee's agricultural land totals lacs of bighas, the total area of agricultural land within a radius of 2 miles from the palace is only 400 bighas including both raiyati and zeeraet land.

8. The real point at issue appears to me, however, to be whether the building in question is required by the assessee as a dwelling house, or as a store house or other out-building by reason of his connection with the land. If it is argued that this building really forms part of the assessee's residence but is built as a separate block primarily for the accommodation of European guests because the social customs of the community to which the assessee belongs prevent him from accommodating such guests in the same building as that in which he himself resides, then this appears to me to raise the larger question, namely, whether the valuation of the whole of the residence of a zamindar should be exempted from income-tax regardless of the relative valuation of that building and his income from landed property. This is a point on which the decision of the High Court is respectfully invited.

I can perhaps make the problem clearer by two illustrations: If a person, whose income derived exclusively from zamindari does not exceed—say 5,000 per annum, has a weakness for erecting a palatial residence with the result that in course of time from his savings he has erected a residence worth—say half a lac of rupees, can he in this case claim exemption in respect of the valuation of that building merely because his income is derived exclusively from zamindari, though there is no reasonable proportion between his annual income from zamindari and the valuation of the building. To take another case: If an assessee has an income of say 5 lacs from zamindari and one lac from investments can he claim exemption in respect of all the buildings on or near the estate on the ground that they are required exclusively for agricultural purposes. It is respectfully submitted that he cannot, and the question which arises namely, the question on the valuation of what buildings or on the valuation of what proportion of the total building or buildings he should be assessed is a question of fact to be decided in each case, regard being had in coming to a decision to the provisions of the proviso to 2 (1) (c) of the Act: in particular to the point whether the building in question or the whole of the buildings are required by reasons of the assessee's connection with the land.

9. Now, the assessee, in this case, does not derive his income exclusively from agriculture and indeed he has been exempted in respect of the valua-

tion of a portion of his Calcutta house on the ground that that house is partly required by him for business purposes. The case of the Department then is that if this building called Chatra Bhawan is required by him, it is not required by him in his capacity as a zamindar or by reason of his connection with agriculture but really by virtue of the position which he holds as a person of great wealth and social position. It is admitted that the assessee has a considerable business in stocks and shares and this business is carried on by him largely from Darbhanga.

10. The building in question is admittedly not required as a store-house.

11. The next question for consideration is whether it is required as an out-building. Presumably, the expression out-building refers to servants' quarters, stables, garages or other buildings of this nature situated at a distance from a main building and subsidiary to it. If this view is correct, this building cannot be classed as an out-building.

12. The next question for decision is whether *Nazrana* or *Salami* paid to a landlord by the raiyat in consideration of the former's recognizing a transfer of a holding, the transfer of which is not recognized by the law or is of doubtful legality is agricultural rent.

13. I understand that in a reference of this sort a full statement of the facts is considered to be my primary duty. In this specific case, however, the formulation of the question appears in itself to state all the facts and it is difficult to add anything of value.

14. These payments are made under the circumstances noted in formulating the question. They are not payments made under any section of the Bengal Tenancy Act and they are admittedly not rent as defined in that Act and the question at issue is whether they are revenue as described in section 2 (1) (a) of the Income-tax Act. This point, as the Court is no doubt aware, has already been discussed on two occasions in the Calcutta High Court, and while in *Birendra Kishor Manikya v. Secretary of State* (1) it was held that such *Nazar* was not agricultural income but was the price paid to the landlord to purchase peace, in *Nawabzadi Mehar Bano Khanum v. Commissioner of Income-tax, Bengal* (2) it was held by a Full Bench that such *Nazar* or *Salami* is revenue and is profit of the land and flows from the ownership thereof, and is accordingly not taxable. Where Judges have disagreed, I must naturally express an opinion with some diffidence. Unfortunately, we have no definition of revenue in any Legislative enactment, but in the latter case referred to above, the learned Judges appear to have based their conclusion that *Nazar* was revenue on the definition of revenue as given in the Oxford Dictionary, namely "the return, yield or profit of any land, property or other important source of income; that which comes into one as a return from property or possessions, specially of an extensive kind; income from any source specially of an extensive kind; income from any source but specially when large and not directly earned". They held that this *Nazar* is money which comes to the landlord by virtue of the fact that he is the owner of the land and viewed in this light, it clearly is derived from the land and is agricultural income. I would respectfully urge that if revenue is taken in this wide sense, the result would be

(1) 1 I.T.C. 67.

(2) 2 I.T.C. 99.

to include within the meaning of agricultural income illegal realisations of *abwabs* which a landlord realizes by virtue of his position as a landlord, though these are neither agricultural rent nor revenue, while royalty derived from minerals would also be on this view non-taxable, if the surface of the land from which the minerals were mined was used agriculturally as is often the case. It is submitted therefore that the learned Judges in that case have accepted much too wide a definition of the word "revenue".

15. The next question for consideration is whether landlords' fees received by a landlord are taxable or not. These fees are realized under section 12 (2) of the Bengal Tenancy Act. They are realized by the Registration Officers from the party on the occasion of the registration of a transfer of a tenure and are fixed on a percentage basis of the annual rent of the tenure. These fees are obviously not rent as defined in the Tenancy Act and the question for decision is whether they are revenue derived from land. They are not derived directly from the land and the real question here, as in the case of *Nazar* discussed above, would appear to be whether revenue is to be defined in the very wide sense in which it is defined in the Oxford Dictionary. My view is that the correct way to view these receipts is to hold that they are not rent or revenue derived from land but are payable by a tenure-holder under a liability incidental to the ownership of the tenure.

K. P. Jayaswal, L. Pugh, Sir Sultan Ahmad and Anirudda Ji Barman,
for the Assessee.

A. B. Mukerji, Government Pleader, for the Crown.

JUDGMENT.

DAWSON MILLER, C. J.:—Two questions arise for determination in this case which comes before us upon a case stated by the Commissioner of Income-tax under section 66 sub-section (3) of the Indian Income-tax Act, 1922.

The first point, in the order in which they are dealt with in the case stated by the Commissioner, is whether the annual value of a guest-house standing in the compound of the assessee at Darbhanga is exempt from income-tax under the provisions of the Act on the ground that it is agricultural income within the meaning of section 2, sub-section (1), clause (c) of the Act. If it falls within that section then it is exempt under section 4, sub-section (3), clause (viii) as being agricultural income. Under section 2, sub-section (1) (c), agricultural income for the purposes of the Act includes any income derived from any building owned and occupied by the receiver of the rent or revenue of any such land (that is, agricultural land) provided that the building is on or in the immediate vicinity of the land and is a building which the receiver of rent or revenue by reason of his connection with the land requires as a dwelling house or as a store-house or other out-building.

The Commissioner has found the facts relating to the house in question from which it appears that the house stands in the same compound as the principal dwelling-house or palace of the Maharajadhiraja of Darbhanga at Dharbhanga. It is used principally for accommodating European guests when they visit him. This, I apprehend, would include not only such guests as might arrive on social occasions but all such as had reason to visit the Maharajadhiraja

officially or on business connected with his estate which is of vast dimensions. The Commissioner has taken the view that under section 2, sub-section (1) (c) of the Act such a house can only be exempt if and in so far as it does not exceed the necessary requirements of the assessee having regard to the position which he holds by reason of being a zamindar deriving his income from land. The view he has expressed is that if in fact he has other sources of income, then this is a matter to be taken into consideration; for income derived from such sources may make him a person of some importance and social position and therefore he may require a larger house than would be the case were he merely a zamindar. He has then considered whether it is necessary for him to have a guest-house at all by reason of the fact that he is the zamindar of the Darbhanga Raj, and as I understand the findings the conclusion he comes to on that part of the case is that he does not require this guest house as a zamindar but merely because he is a person of great wealth and social position. It is perhaps not irrelevant to observe that the wealth and social position of the assessee arise from the fact that he is the proprietor of the Darbhanga Raj the largest zamindari in this Province and perhaps one of the largest in India. The way the Commissioner puts the case is this:

"Now the assessee in this case does not derive his income exclusively from agriculture and indeed he has been exempted in respect of the valuation of a portion of his Calcutta house on the ground that that house is partly required by him for business purposes. The case of the Department then is that if this building called Chatra Bhawan is required by him, it is not required by him in his capacity as a zamindar or by reason of his connection with agriculture but really by virtue of the position which he holds as a person of great wealth and social position. It is submitted that the assessee has a considerable business in stocks and shares and this business is carried on by him largely from Darbhanga".

From that it may be assumed, I think, that the finding of the Income-tax Commissioner was that the house was not required as a dwelling house by the assessee within the meaning of section 2, sub-section (1) (c) of the Act, because his income was not derived exclusively from zamindari but also from other sources. In fact it appears from his statement of the case that the Commissioner would consider in each individual instance whether a dwelling-house owned and occupied by a landowner was in fact larger or more commodious than might be considered necessary for his requirements as a landowner, and if he should consider that it was, then he would assess a certain proportion of the annual value of his house to income-tax. That proportion would depend, according to the view taken by the Commissioner, upon the relation between the assessee's income derived from his estate and that derived from other sources, and would necessarily vary from time to time as his savings increased or diminished. It is not disputed that the building is owned and occupied by the assessee and as I understand the findings of the Commissioner it is conceded that the Maharajadhiraja of Darbhanga as the Zamindar of a large Raj does require a dwelling-house in that locality by reason of his connection with land; and further it is not disputed, as I understand it, that the building is on or in the immediate vicinity of the land forming the Darbhanga Raj. It is also a matter of common knowledge that amongst persons of the religion to which the Maharajadhiraja belongs it is not convenient to accommodate his guests within his own dwelling-house and therefore for this purpose there is a separate house set

apart near his principal dwelling house for their accommodation and in this respect I consider that the matter must be approached from the point of view that it makes no difference whether the guest-house is really a part of the main dwelling-house itself or is structurally unconnected with it. It is by no means unusual in this country, especially in the case of large and even moderately large houses, to find a guest house attached thereto.

The question which we have to decide is not, in my opinion, purely one of fact. It has been argued on behalf of the Commissioner that this really is a question of fact of which he is the sole Judge, but in dealing with the matter it seems to me that he has not properly construed the section, and has applied a test to this case which is not the proper test to be applied. If the Commissioner's view is to be accepted then he would be equally entitled to consider in each case whether a particular house owned by a zamindar, for which exemption from tax was claimed, was larger than was actually sufficient to supply his needs having regard to the fact that he was a zamindar. It would be for the Commissioner to say whether he was entitled to this or that extra room, whether he was entitled to have stables, for example, to accommodate so many horses, and in each case if the question is to be regarded merely as one of fact the Commissioner would be the sole Judge whether the house was or was not sufficient for the minimum requirements of the assessee. That to my mind is not the intention of the Act. I have referred to the terms of the section, and in my opinion the proper construction is this. Once it is shown that by reason of the assessee's connection with the land he requires a dwelling-house in that vicinity then we are not concerned to enquire whether the dwelling-house is more commodious than other persons in the same position would consider sufficient for their actual needs, a matter about which opinion might widely differ. The intention of the Act seems to me to have been that if by reason of his connection with the land the assessee does require a dwelling-house and it is admitted in this case—at all events no argument has been adduced to the contrary—that he does require a dwelling-house in Darbhanga, then the section is complied with in so far as the question of his requirements is concerned and it is not open to the Commissioner to consider whether the particular class of house is more or less than the actual requirements of a zamindar in his position according to some standard which may vary from time to time in the opinion of different Income-tax Commissioners. For these reasons I think that upon the facts found it must be held that a dwelling-house being required in this place, and the house in question being regarded as part and parcel of such a dwelling-house, and it being also admitted that the dwelling-house is required by reason of the connection of the assessee with the land, then the provisions of the section are complied with and the assessee, in my opinion, is exempt from tax.

The next point is one which has recently been the subject of a decision of a Full Bench of the Calcutta High Court. Stated shortly the point is whether what is called mutation fees, that is to say, fees paid by the transferee of a non-transferable occupancy holding and fees paid by the transferee of a tenure, known as landlord's fees, under section 12 of the Bengal Tenancy Act, are exempt as being included in the definition of agricultural income in section 2 of the Act. The definition there contained includes amongst agricultural income any rent or revenue derived from land which is used for agricultural purposes and is either assessed to land revenue in British India or subject to a local rate assessed and collected by officers of Government as such. It is not

disputed here that the land in question comes within the description mentioned in that section. The contention is however that the fees derived from the sources which I have mentioned will not come under the description of rent or revenue derived from land. The contention on behalf of the Crown is that at all events in the case of fees paid by the transferees of a non-transferable occupancy holding, these are not in any sense of the word rent or revenue derived from land; they do not arise out of the creation of a new tenure in which case sometimes a premium or *salami* is paid in advance which may be taken to represent a consolidated sum of rent in addition to the annual rent payable, but it is said that the money is something in the nature of damages for a breach of contract or, as stated in the judgment of Mookerjee J in *Birendra Kishor Manikya v. Secretary of State for India* (1) money paid in order to secure peace and therefore not to be regarded as revenue derived from land. The case to which I have just referred was the subject of consideration in the later case of *Nawabzadi Meher Bano Kanum v. Commissioner of Income-tax, Bengal* (2). In that case the decision of Mookerjee J in the earlier case was overruled and it was held that *salami* or *nazar* paid by a tenant to a landlord for his recognition as a tenant of a non-transferable holding is rent or revenue within the meaning of section 2. (1) (a) of the Indian Income-tax Act and is therefore exempt from taxation. The real question I think for determination upon this part of the case is whether these fees paid by the tenants are to be regarded as income or revenue derived from land. Whether they be something in the nature of damages, although that clearly is not an appropriate term to use in this connection, or whether there is any breach of contract by the transferee, or whether they may be regarded as something paid for the purchase of peace, seems to me to be altogether beside the question. It may just as appropriately be said that rent itself, when it is in arrears, or when there is any dispute about the liability to pay it, may be paid to purchase peace, and so here it is undoubtedly a fact that, just as in the case of rent, the sum is payable by a tenant to his landlord solely by reason of their relationship as tenant and landlord of land and whether it has the effect of purchasing peace or not seems to me to be entirely immaterial to the question under consideration. It arises by reason of the tenant being given the use and occupation of the land which without it he could not acquire. The term 'revenue' as given in the Oxford Dictionary has been set out at length in the judgment of the Full Bench of the Calcutta High Court to which I have just referred. It is unnecessary to repeat it but it seems to me that it clearly includes payments of this nature and according to the ordinary general use of the term I think also that it must include payments by the tenants of land owned by the landlord for the transfer to them of holdings or tenures, and I entirely agree with the conclusions arrived at by the majority of the Court in the case of *Meher Bano Khanum v. Commissioner of Income-tax, Bengal* (2). That this particular class of revenue is derived from land I do not think for a moment can seriously be disputed. These payments are so intimately connected with the ownership of land and are payable by the tenants in the same way as rent is payable that to my mind it is impossible to come to any other conclusion than that they are revenue derived from land.

(1) 1 I.T.C. 67.

(2) 2 I.T.C. 99.

For these reasons I think that upon both these points the assessee is entitled to exemption from tax.

This opinion may be forwarded to the Income-tax Commissioner for his guidance.

We assess the hearing fee in this case including the printing of the paper book which we understand is approximately Rs. 150 at Rs. 300.

ROSS J.—I agree.

[246] IN THE HIGH COURT OF JUDICATURE AT BOMBAY.

Before Sir Amberson Marten, Kt., Chief Justice and Mr. Justice Kemp.

[20th March, 1928.]

The Remington Typewriter Company, (Bombay) Limited as agent
of the Remington Typewriter Company of New York ... *Assessees.**

v.

The Commissioner of Income-tax, Bombay Referring Officer.

Income-tax Act (XI of 1922), Secs. 40, 42, 43 and 66 (2)—Non-resident company—Indian Companies formed by non-resident company at Bombay, Madras and Calcutta for sale of its goods—Non-resident company holding all the Indian Companies' shares—Profits of Indian Companies paid as dividend to non-resident company—Assessment on Bombay company as agent of non-resident company on latter's manufacturer's profits on goods sold in India—Assessment of super-tax on Bombay company as agent on dividends of the Indian Companies—Legality of the assessments—Proper mode of assessing super-tax—Statement of the case—Jurisdiction of Commissioner to find facts, observations on.

The Remington Typewriter Co. of New York formed three limited companies in India—The Remington Typewriter Co. (Bombay) Ltd., The Remington Typewriter Co. (Madras) Ltd. and the Remington Typewriter Co. (Calcutta) Ltd.—and sold to them the business of selling its typewriters and goods in their respective areas, the consideration for the sale being the allotment of all their shares to the New York Company. The business of these subsidiary Indian Companies was to purchase typewriters from the New York Company at the usual wholesale discount prices and to sell them in India, the profits arising therefrom, less income-tax, being distributed as dividends to the New York Company. The Income-tax Officer alleging that besides the dividends, the New York Company had made a manufacturer's profit of 5 per cent on the sale of its goods, assessed the Bombay Company as agent of the New York Company under section 42 of the Income-tax Act, to income-tax and super-tax in respect of this manufacturer's profit and to super-tax on the dividends payable to the New York Company on its shares in the three Indian Companies. On a case stated under section 66 (2) of the Act on the legality of this assessment,

Held, (1) that the Bombay Company was not in receipt on behalf of the New York Company of the alleged manufacturer's profit and consequently was not assessable thereon under section 42 of the Act,

* (1928) I.L.R. 52 Bom. 726; 30 Bom. L.R. 1190; A.I.R. (1928) Bom. 465.

(2) that the Bombay Company which has nothing whatever to do directly or indirectly with any dividends on the shares of the Madras and Calcutta Companies, was not assessable to super-tax on those dividends not received by it within the meaning of section 40,

(3) that the Bombay Company could not be assessed to super-tax in respect of the dividends on its own shares, as it did not receive those dividends "on behalf" of its shareholders, the New York Company, within the meaning of sections 40 and 42 of the Act, and

(4) that the Bombay Company had a business connection with the New York Company so as to constitute the former an "agent" of the latter within the meaning of section 43 of the Act.

Imperial Tobacco Co. v. Secretary of State for India 1 I.T.C. 169; *Bombay Trust Corporation v. Commissioner of Income-tax, Bombay* 3 I.T.C. 135. *Followed.*

Obiter. Under the amended sections 57 and 58 of the Act, the appropriate amount of super-tax on the dividends of the Indian Companies should be deducted by the principal officer of each company concerned.

Observations on the limits of the jurisdiction of the Commissioner to find facts in stating a case to the High Court under section 66 (2) of the Act.

Case [Civil Reference No. 19 of 1927] stated under section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bombay for the opinion of the High Court.

CASE.

Under section 66 (2) of the Indian Income-tax Act, 1922, (XI of 1922, India); (hereinafter referred to as the Act) and at the instance of the Remington Typewriter Company (Bombay) Limited, (hereinafter referred to as the assessee), I have the honour to submit for favour of your Lordships' opinion the questions of law categorically set out in para 9 below *re*: the interpretation of sections 42 (1) and 43 of the Act, arising out of the income-tax and super-tax assessments of the above assessee for the years 1925-26 and 1926-27 as agent of the Remington Typewriter Company of New York (hereinafter referred to as the New York company).

2. *Facts of the Case*:—The Remington Typewriter Company of New York is a company incorporated in the United States of America and doing business as manufacturers and sellers of the well-known Remington Typewriters and accessories for the same. It has formed in India three limited companies as under:—

- (1) The Remington Typewriter Co. (Bombay) Limited,
- (2) The Remington Typewriter Co., (Madras) Limited, and
- (3) The Remington Typewriter Co., (India) Limited.

All the shares in these companies are held by it excepting three shares of Rs. 10 each which are held by its nominees who appear to be its employees in India. Thus the Remington Typewriter Company (Bombay) Limited, has a capital of six lakhs divided into 60,000 shares of Rs. 10 each and the New York company holds all of them excepting three which are held by its em-

ployees. Two of these three shareholders are Mr. F. J. Hull, who is styled the Managing Director for all the three Indian companies, and Mr. Z. Haque who is said to be his Secretary. The third share is in the name of the local manager who is styled a Director. Messrs. Hull and Haque are also two of the three shareholders in the other two Indian companies too, the third shareholder being the local Manager for Madras or Bengal as the case may be.

3 The assessee looks to the business of selling Remington Typewriters and goods in the Bombay Presidency, Central Provinces, and certain other adjoining portions of India. The Remington Typewriter Company (Madras) Limited, looks to this business in the Madras Presidency including Mysore and other adjoining parts of India. The Remington Typewriter Company (India) Limited, looks to the business in Bengal and the remaining parts of India.

4. It is alleged that there is no trade agreement between the New York Company and any of the above three Indian companies but that each of the latter is allowed a 40 per cent discount on all goods sent to it for sale. The net profit earned by each of these companies is finally carried away by the New York company in the shape of dividends paid to it as a shareholder.

5. It is not necessary for the purpose of this reference to state at length the history of the formation of the above companies. Suffice to say that in December 1921, the New York company formed a limited company here calling it the Remington Typewriter Company (Bombay) Limited (the assessee) and by an agreement dated 18—1—1922 (copy annexed as Exhibit A*) sold to it the business of selling Remington Typewriters and goods in the Bombay Presidency and certain adjoining parts for a sum of Rs. 6,00,000 payable in shares of this company. Thus the Bombay Company (the assessee) came into existence with a capital of six lakhs divided into 60,000 shares of Rs. 10 each which were all issued to the New York company which transferred three of them to its nominees viz., its employees as stated above. A copy of the Memorandum and Articles of Association of this company accompanies as Exhibit B*. From Exhibit A, it will be seen that Mr. F. J. Hull has signed it both for the New York company as well as for the assessee. The Madras company came into existence under exactly similar circumstances. As regards the Remington Typewriter Company (India) Limited, it came into existence in 1914 taking over the Indian business from the Remington Typewriter Company (England) Limited and allotting 9,996 out of its 10,000 shares of Rs. 10 each to the New York company as nominee of the English company. It too belonged of course wholly to the New York company. It carried on its business in the whole of India upto the end of the year 1921 when the New York company purchased from it as per agreement dated 12—12—1921, (copy annexed as Exhibit C*) the Bombay and Madras businesses and sold them to the Bombay and Madras companies as stated above leaving the Bengal and the rest of India to the India company. All these purchase and sale agreements in reality appear to be mere paper transactions, the purchaser and seller being one and the same party viz., the New York company which always was and continued to be the sole owner of the total Indian business whether under the style of the original Remington Typewriter Company (England) Limited or the all-India company or the three companies now in existence.

6. Finding that the whole of the Indian business in reality belonged to the New York company, the Senior Income-tax Officer taxed it on the profits of all the companies combined plus 5 per cent in addition on sales on account of profit made here by the New York company but not included in the profit shown by the three Indian companies. He took it that the purchase price at which the local companies were made to purchase the Remington goods from the New York company was fictitious and not the actual cost to it. Thus if a typewriter were shown as sold by the assessee for Rs. 300 making a profit of Rs. 100 the alleged purchase price being Rs. 200, the Senior Income-tax Officer took it that the real cost to the New York company was Rs. 190 only and that therefore the actual profit earned by it was not Rs. 100 alone but that sum plus Rs. 10. The assessee was given an opportunity to prove by actual figures that this much extra profit did not accrue to the New York company from sales here but it did not avail itself of it. As the New York company was a non-resident company, for the purposes of assessment, the Senior Income-tax Officer treated the assessee as its agent within the meaning of section 43 of the Act and taxed it on the total income arrived at as above.

7. Against the above assessments, the assessee appealed to the Assistant Commissioner saying that there was no business connection between it and the New York company and that it was not its agent and so could not be taxed as such. The Assistant Commissioner dismissed the appeal. He was of opinion that there could not be a case in which there was closer business connection between two parties than in the present case and that not only was the assessee the agent of the New York company but that, as a matter of fact, the two were identically the same.

8. Not satisfied with the Assistant Commissioner's decision, the assessee has applied to me for this reference to the High Court.

9. *Questions for the decision of the High Court:*—The questions of law which the assessee wants your Lordships to decide are stated by it as under:—

(1) Whether the profit of the Remington Typewriter Company of New York upon goods exported to British India are or can be held to be chargeable to income-tax and super-tax under section 42 (1) of the Act or otherwise.

(2) Whether super-tax upon dividends received by the Remington Typewriter Company of New York from the Remington Typewriter Company (Bombay) Limited, the Remington Typewriter Company (India) Limited, and the Remington Typewriter Company (Madras) Limited, can under section 42 (1) of the Act or otherwise be charged against and collected from an agent.

(3) Whether the Remington Typewriter Company (Bombay) Limited, is or can be held to be the agent of the Remington Typewriter Company of New York under section 43 of the Act.

10. As section 66 (2) of the Act requires me to give my opinion while submitting the reference to your Lordships, I beg to state as under:—

11. *Opinion of the Commissioner:*—The sections of the Act with which we are concerned in this case are 42 (1) and 43. Taking up section 42 (1) first, it runs as under:—

“42. (1) In the case of any person residing out of British India, all profits or gains accruing or arising to such person, whether directly or indirectly through or from any business connection or property in British India, shall be deemed to be income accruing or arising within British

India, and shall be chargeable to income-tax in the name of the agent of any such person, and such agent shall be deemed to be, for all the purposes of this Act, the assessee in respect of such income-tax:

Provided that any arrears of tax may be recovered also in accordance with the provisions of this Act from any assets of the non-resident person which are, or may at any time come, within British India."

It clearly lays down that in the case of a person residing out of British India, all profits and gains arising directly or indirectly, through or from any business connection or property in British India, shall be deemed to be income accruing or arising within British India and charged to tax in the name of the agent of the non-resident person. In the present case, the non-resident person is the New York company. The profits for which tax has been levied are those received by it ostensibly by way of dividends from the three Indian companies formed by it and of which it is the sole owner and 5 per cent more on the value of goods sent by it for sale here through the three Indian companies. Taking up dividends first, the word "property" in this section 42 (1) has its ordinary meaning and includes moveable as well as immoveable property. There is no definition of this word in the Act or in the General Clauses Act and so it must be taken to have been used in its ordinary sense. The shares which the New York company has in the three Indian companies merely represent the money invested by it in them and are no doubt part of its moveable property and the dividend income which it gets is the result of this investment. Hence under section 42 (1), the dividend income is to be deemed to accrue and arise in British India. As a matter of fact, in all cases, dividends from companies in British India do actually accrue and arise in British India and nowhere else being the result of money invested in companies doing business in British India. Hence not only have these dividends to be deemed to accrue or arise in British India, but they actually do accrue and arise here. Nothing can be plainer than this and it is sheer waste of time to attempt to prove anything otherwise.

12. Again, if we look to the real position in the case, these dividends are nothing but profit arising from business done by the New York company itself in British India. It and the Indian companies mean really one and the same party without any doubt. The business which the Indian companies are ostensibly supposed to do is really done by the non-resident New York company and no one else. Having created the fiction of companies, the profit is drawn by way of dividends but that does not in the least debar the Crown from enquiring into the real nature of the transaction and taking the profits arising therefrom to have been made by the person by whom they have really been made as per your Lordships' decision in the case of *Sir D. M. Petit, Bart. v. Commissioner of Income-tax, Bombay* (1). The Indian companies have as a matter of fact no independent existence whatsoever. How is business really carried on here? It is done through Mr. F. J. Hull, who is styled the Managing Director of all the Indian companies and the local managers of the offices at Calcutta, Madras and Bombay styled Directors. Who appoints the Managing Director and the Directors? Who can turn them out and whose instructions are they bound to follow? Ostensibly they are appointed by and are under the

sole control of the shareholders of the Indian companies but these shareholders mean absolutely nothing but the New York company itself. Hence it is this company which does the whole business here and no one else. Take it in whichever way we like, these dividends are nothing but income, profits and gains accruing and arising directly from not merely a business connection but business itself in British India and property in British India *viz.*, the capital invested in the business here by the New York company. Hence section 42 (1) undoubtedly applies.

13. As regards the additional profit at 5 per cent on sales in British India, it is on exactly the same footing since as stated above, every one can very plainly see that it is the New York company which is undoubtedly doing business in British India and not the three Indian companies created by it and which solely belong to it. The total invoice value of goods shipped by it to British India in 1925-26 was as much as Rs. 13,93,528 and on it 5 per cent additional profit has been charged by the Senior Income-tax Officer, taking it that the real cost of the goods sent was only 95 per cent of this sum. The assessee does not wish to challenge this rate of additional profit. Having powers to revise a subordinate authority's orders under section 33 of the Act, I offered to go into the question whether the New York company did earn 5 per cent more over and above the profit earned through the Indian companies, provided the New York Balance Sheet and Profit and Loss Accounts were produced but was informed that this could not be done and that the 5 per cent rate would be accepted if your Lordships were pleased to decide the questions referred to you against the assessee. The only inference in the circumstances is that this extra profit (if not something more) is really being made here. It is made through the Indian companies and, to say the least, arises from the business connection which the New York company has in British India. Where on the face of it, a non-resident company creates for the purposes of pushing the sale of its goods in British India, three Indian companies of which it is admittedly the sole owner and carries on the business of selling its goods through them, surely there is much more than a business connection in British India. It is actually doing business here without any doubt as stated in the foregoing paras. Holding as it does all the shares in the Indian companies but 3 of Rs. 10 each which too are held by its employees, the whole power is positively centered in it, which it exercises through Directors appointed by it. Everything that is done in India is under its sole control as under the Articles of Association of the companies formed by it, all power is centered in the shareholders and all shares are virtually held by it. Hence the 5 per cent extra profit too undoubtedly accrues from a business connection as well as business in India.

14. As the income under assessment thus accrues and arises from a business connection and business and property in British India, it falls under section 42 (1) and has to be assessed "in the name of the agent of the non-resident" as required by it. This disposes of questions (1) and (2).

15. As regards question (3), the term "agent" is used in section 42 (1) of the Act not in its ordinary sense but has a special meaning as defined in section 43 of the Act which follows it and which runs as under:—

"43. Any person employed by or on behalf of a person resident out of British India or having any business connection with such person, or through

Agent to include persons whom such person is in the receipt of any income, profits or gains upon whom the Income-tax Officer has caused a notice to be served of his intention of treating him as the agent of the non-resident person, shall, for all the purposes of this Act, be deemed to be such agent:

Provided that no person shall be deemed to be the agent of a non-resident person, unless he has had an opportunity of being heard by the Income-tax Officer as to his liability."

The meaning of the term has been intentionally extended for the purposes of the Act as stated in the section itself and made to include *inter alia* "any person having any business connection with a non-resident person or through whom such person is in receipt of any income, profits or gains." In the present case, the Senior Income-tax Officer has determined the assessee i.e., the Remington Typewriter Company (Bombay) Limited, to be the agent of the New York company. If the former has any business connection whatever with the latter or if it be in receipt of any income, profits or gains through the latter, the Senior Income-tax Officer's action is correct. Hence we will first see whether any business connection does or does not exist. What is the Bombay company (the assessee) for? It is merely a creation of the New York company for the purpose of selling its goods here with a view to earn profit. I cannot think of a case in which business connection can be closer. In fact not only has the assessee a clear business connection with the non-resident but is identical with it. Hence the Senior Income-tax Officer has rightly treated the assessee as the agent of the New York company.

16. Not only has the New York company the closest connection with the assessee but it is undoubtedly in receipt of income, profits and gains through it. The word "through" in this section 43 of the Act means "by means of" or "by the instrumentality of" and what has already gone before leaves no doubt that the non-resident company is in receipt of income, profits and gains by the instrumentality of the assessee.

17. To support its contentions, the assessee says that it is not in receipt of any income on behalf of the New York company within the meaning of section 40 and so cannot be treated as its agent as per the decision of the Calcutta High Court in the case of the *Imperial Tobacco Company of India Ltd., v. The Secretary of State* (1). In the first place, this case of the Imperial Tobacco Co., referred to an assessment under the old Income-tax Act of 1918 (Act VII of 1918, India). In it the word 'agent' was defined in its section 34 but that section was not the same as section 43 in the present Act which is under consideration before your Lordships. There is a very important difference between these two sections in that the latter contains the additional words "or through whom such person is in the receipt of any income, profits or gains" which did not find a place in the former. As a shareholder in a company does get his dividend *through* it, the omission of these words in section 34 of the Act of 1918 deprives the case of all its force when sought to be followed in a case falling under section 43 of the present Act. Also the present case has nothing in common with that case of the Imperial Tobacco Company where the question was between a *bona fide* shareholder and a com-

pany and not a sham company and another company which created it and which was its sole owner. Also the word "agent" is clearly defined in section 43 of the Act and as long as that section does not at all refer to section 40, it is not understood how the latter section can at all come in. These sections 40 and 43 occur in Chapter V of the Act which deals with "Liability in Special Cases." There are various kinds of these "Special Cases," some of which fall under section 40, some under section 41, some under section 42 (1) and some under section 42 (2). Section 40 merely lays down that in the case of an agent of a non-resident person in receipt of any income, profits or gains on behalf of the latter, he is to be charged in place of the latter. It does not at all say that in no other case is a non-resident to be charged through an 'agent'. On the contrary, there is below it, section 42 (1) which deals with cases in which a non-resident may not be in receipt of income through an agent. It refers expressly to cases of income accruing or arising directly or indirectly through or from business connection or property in British India and says that in such cases, the income is to be charged in the name of the agent of such person and it is section 43 which defines what persons are to be treated as agent and that section is in no way dependent on section 40. As far as the meaning of the word "agent" is concerned, as it is section 43 which defines it and not section 40, we have to look to it (section 43) alone. The incorrectness of the proposition propounded on behalf of the assessee can be easily seen from the fact that if only a person in receipt of income on behalf of a non-resident is to be treated as his agent, the whole of section 43 becomes otiose. What is the use of it at all, if an agent is to be none else but a person in receipt of income on behalf of the non-resident? Why drag in at all in section 43 persons employed by the non-resident person as also persons having business connection with him etc? With the greatest deference, I submit therefore that it is quite irrelevant to drag in section 40 in this case when it has nothing to do with it. Of course, in this particular case, the assessee happens to be in receipt of income on behalf of the New York company because the profits which it receives are the profits of the New York company and no one else including the 5 per cent extra profit too charged by the Senior Income-tax Officer which too is primarily received here as soon as it gets the sale price of the typewriters and goods sent by the New York company. However, the Crown does not at all wish to lay any stress on this point as I respectfully maintain that section 40 has nothing to do with this assessment.

18. Another argument advanced is that as under section 57 (2) of the Act, the Principal Officer of a Company has to deduct super-tax in the case of a non-resident shareholder, the Legislature did not intend that a company be treated as the agent of its shareholder under the Act and that the relation of a company and a shareholder was not "business connection." As stated so often above, this is not at all merely a question of a company and a shareholder. It is a question in which a non-resident company is actually doing its business here and has for that purpose created a local company which entirely belongs to it and so whatever is done here is under its sole control. Turning to section 57 (2) itself, the Legislature has under it really gone much beyond merely making a company an agent of a shareholder. It has actually required it through its Principal Officer to first deduct super-tax before paying a dividend to a non-resident shareholder. This is a much shorter cut to get revenue than making the company or its Principal Officer the agent of the non-resident person and levying an assessment through him after calling for a return of income, examin-

ing proofs *re*: income earned, passing an assessment order, issuing a Demand Notice and then collecting the tax due.

19. Another argument advanced is that the term "business connection" in section 43 in a literal sense does include the relation of buyer and seller but that if section 43 were to be so construed, it would lead to absurd results. In this case, it is not at all a question of the relation of a buyer and seller. Here the non-resident is doing here its own business of selling goods manufactured by it through the medium of a company owned by it exclusively. The assessee *viz.*, the Bombay Company is not merely a buyer. It is part and parcel of the New York company itself and is identical with it. It is not at all an independent buyer having no connection with the seller. It is identical with the seller without the least doubt. In the circumstances, it is no use pursuing this argument further.

20. It is further alleged that "agent" in section 43 should be interpreted as having its ordinary meaning or the meaning assigned to it in section 230 (1) of the Indian Contract Act. If the word "agent" was used in the ordinary sense in the Income-tax Act or had the same meaning as in section 230 (1) of the Indian Contract Act, where was the necessity to put in section 43? It is precisely because the Legislature has not used the word "agent" either in its ordinary sense or in the sense in which it is used in the Indian Contract Act that it has put in section 43 stating clearly what is included in this term.

21. The case of the *Secretary, Board of Revenue, Madras v. The Madras Export Company* (1) has been also cited by the assessee but it as well as the case of the Imperial Tobacco Company referred to above have nothing to do with this case in which a non-resident company is doing here in British India its own business through resident companies created by it and owned solely by it.

22. It is further argued that the word "property" in section 43 means immovable property only and does not include shares because the word 'property' as is shown by section 9 means immovable property. What this means I fail to understand. Section 9 does not define the word "property". It merely says that "tax shall be payable by an assessee under the head "property" in respect of the *bona fide* annual value of property consisting of any building or lands appurtenant thereto etc....." For the purposes of the Act, 'taxable income' is divided into six heads and one of these is styled "Property" and under it income from immovable property is classified but that does not mean that wherever the word "property" occurs in the Act, it means immovable property only. Were it so, the exemption allowed to income devoted to charitable or religious purposes under section 4 (3) (i) of the Act would be greatly curtailed and confined to income from immovable property which would be most unjust as income from shares and securities is so often devoted to charitable or religious purposes.

23. It is further argued that in view of the provisions of sections 57 (2) and 58 (2), super-tax can only be deducted at source by the Principal Officer or be charged direct to the shareholder and cannot be assessed through an agent under section 43. This is wholly incorrect as section 58 (1) makes sections 42 and 43 of the Act applicable to super-tax too and section 57 (4) expressly lays down that when super-tax has been deducted at source by a Principal Officer

under section 57 (2), "credit shall be given therefor in determining the amount of the tax to be payable by an agent of such a non-resident person under the provisions of sections 42 and 43." Nothing can be clearer than this to disprove the arguments advanced on behalf of the assessee.

24. It is further alleged that the assessee under its Memorandum of Association is entitled to carry on business of manufacturers and dealers in typewriters etc., without any restriction and that it has actually obtained supplies from the Tod Photograph Company and others. This argument loses its force entirely if we merely bear in mind the fact that it is the New York company which has a real existence and which is doing business here under the name and style of the Remington Typewriter Company (Bombay) Limited. It might make here some petty purchases from others in case of need but that makes no difference. The total value of such purchases in 1925-26 was only Rs. 36,217 out of total purchases amounting to nearly 14 lakhs of rupees.

25. For all the above reasons, my Lords, I am respectfully of opinion that the answers to all the questions put must be in the affirmative.

26. A copy of your Lordships' decision may kindly be certified to me for further action as required by section 66 (5) of the Act.

Taraporewala with the Solicitor to Government, for the Crown.

Bhulabhai J. Desai with Messrs. *Crawford Bayley & Co.*, for the Assesseees.

JUDGMENT.

MARTEN C. J.:—In this income-tax reference the Remington Typewriter Company (Bombay) Limited, (whom I will call "the Bombay Company"), have been assessed under section 42 (1) of the Indian Income-tax Act, 1922, as agents of the Remington Typewriter Company of New York, (whom I will call "the American Company"), for the years 1925-26 and 1926-27 in respect of profits alleged to have accrued or arisen to the American Company through their business connection with the Bombay Company, including alleged profits in connection with the Remington Typewriter Company (Madras) Limited, (whom I will call "the Madras Company"), and the Remington Typewriter Company (India) Limited, (whom I will call "the Calcutta Company").

2. The case for the Crown before the Income-tax Officer and the Assistant Commissioner appears to have been based on the view that the Bombay Company and the American Company were separate entities in substance as well as in law, but that the former was an agent for the latter within the meaning of section 43 by reason of the close business connection between these two companies. This will be found *inter alia* from the points of argument before the Assistant Commissioner and the latter's judgment Exhibit E following on the petition and grounds of appeal to the Assistant Commissioner of the 28th March 1927 Exhibit D. This order of the Assistant Commissioner could not be and was not appealed against to the Commissioner having regard to the limited nature of the right of appeal given by section 32 of the Act. And it is common ground that the Commissioner did not exercise his powers of review under section 33, apart, it is said, from some slight correction made in certain figures.

3. It would appear then that up to the conclusion of the proceedings before the Assistant Commissioner, there was no suggestion that the Bombay company

was a mere *alias* for the American Company, or that in fact its business belonged to and was being carried on by the American Company. If there had been any such suggestion, then it would surely have occupied a prominent place in the grounds of appeal Exhibit D, and the points of argument annexure A, and the statement of Mr. Partridge, annexure B to the order of the Assistant Commissioner, Exhibit E. It would also have been dealt with in the latter's judgment.

4. Indeed it is on this basis viz., that the two Companies are separate in substance and in law, that the three questions of law submitted to us have been raised. Accordingly in the first instance I will proceed to deal with the case on that footing. That being so, we have to consider whether the Bombay Company has a business connection with the American Company and is consequently the agent of the American Company within the meaning of section 43 of the Act? And if so, whether the Bombay Company can be assessed under section 42 in respect of the "profits or gains accruing or arising to the" American Company "whether directly or indirectly through or from" that "business connection."

5. For the moment I will assume that the first point should be answered in the affirmative. Then the second point raises the same question of construction which we had to decide in the *Bombay Trust Corporation Ltd., v. Commissioner of Income-tax, Bombay* (1) which was argued immediately before the present case, but in which we reserved judgment until we had heard the arguments in the present case. We have now delivered judgment in the Hongkong Corporation case, and have held that sections 40, 42 and 43 of the Act must be read together; that section 42 only explains or extends the meaning of profits or gains in section 40, as does section 43 of the meaning to be given to the word "agent" in section 40 and elsewhere in the Act, but that the necessity imposed by section 40 of the agent in question being "in receipt on behalf of" the non-resident of the profits chargeable under the Act, applies also to section 42. Shortly stated then we have held that to make an agent chargeable under section 42 he must be in receipt of the income in question on behalf of the non-resident. That decision applies of course to the present case, the material facts of which are briefly as follows:—

6. On the 19th December 1921 the Bombay Company was incorporated in Bombay to take over the Bombay business of the American Company. Its memorandum and articles of association are Exhibit B. Then by an agreement of the 18th January 1922, Exhibit A, the American Company agreed to sell to the Bombay Company its goodwill in a defined territory (which included Bombay and certain other areas) and also its interest in any land in that territory, and all plant, machinery patents, licenses, stock and utensils and all book debts and the benefit of pending contracts, and all cash and other property to which the American Company was entitled in the said territory. The purchase price payable by the Bombay Company was Rs. 6 lacs payable in fully paid shares. The Bombay Company was also to pay all the debts of the American Company in the said territory and to indemnify the latter against the same. The purchase was to take effect as from the 30th November 1921 and was to be completed not later than 30th January 1922.

7. This agreement was duly carried out, and accordingly in substance the whole of the share capital of the Bombay Company was allotted to the American Company, or its nominees, and it is common ground that that share capital is now held by the American Company with the exception of one share held by Mr. Haque'a Secretary, and one share held by Mr. F. J. Hull, and one share by Mr. C. H. Partridge, who are the two directors of the Bombay Company under article 77 of the Articles of Association, Exhibit B.

8. The Bombay Company has ever since been carrying on business in the territory defined by the sale agreement. Its main business is the purchase and sale of the well-known Remington typewriters. Naturally for this purpose they purchase the machines from the manufacturers, the American Company: but some other goods required for their business such as typewriter paper they may purchase elsewhere. According to the evidence before the Assistant Commissioner and in particular the statement of Mr. Partridge, the Bombay Company purchases these Remington Typewriters on the same terms on which they are sold to dealers in other parts of the world, *viz.*, subject to a trade discount of 40 per cent. off the catalogue price to the public. There is nothing sinister in a discount of this nature. It is a common incident of business with manufacturers. Before us counsel for the Bombay Company went one step further, and said that in fact the goods purchased are paid for in New York, and that delivery is effected there. I do not, however, find that expressly stated by Mr. Partridge. It is, however, stated in para 5 of the grounds of appeal Exhibit D that the Bombay Company buys at the American Company's "regular export price as fixed for all dealers throughout the world.....It pays in dollars in New York for goods supplied as invoiced and independently of profit or loss on resale in India."

9. I will now say a word as to the alleged profits for which the Bombay Company has been assessed as agent. The American Company has of course received the dividends on the shares it holds in the Bombay Company. Income-tax has already been deducted on those dividends, and accordingly no question arises as regards the income-tax on those dividends. But what the Crown alleges is that apart from its profit by way of dividends in the Bombay Company, a manufacturer's profit, which has been assessed at 5 per cent, has also been made by the American Company in respect of the goods sold by it from time to time to the Bombay Company. The Crown claims that the Bombay Company as agent is liable to be assessed under section 42 in respect of this manufacturer's profit. The Crown further claims that the Bombay Company as such agent is liable for super-tax not merely on the dividends on the Bombay shares, but also in respect of the dividends payable to the American Company in respect of its holdings in the Madras and Calcutta Companies.

10. Taking first the manufacturer's profit of 5 per cent, the precise figure is not disputed. But as regards the liability of the Bombay Company to pay it, that is clearly concluded against the Crown by our decision in the Hong-kong Corporation case. It was faintly suggested before us that the Bombay Company was in receipt of this manufacturer's profits. But in my judgment that is a hopeless contention. A particular purchase price may well include a profit to the vendor. But it is the vendor who receives that profit and not the purchaser. Consequently I would hold that in the present case the Bombay

Company was not in receipt on behalf of the American Company of this manufacturer's profit of 5 per cent, and consequently cannot be assessed under section 42 of the Act.

11. As regards the alleged liability of the Bombay Company to super-tax in respect of the dividends on the shares of the Madras and Calcutta Companies, the case for the assessee is, if possible, even stronger. The Bombay Company has had nothing whatever to do directly or indirectly with any dividends on the shares of the Madras Company or the Calcutta Company. Therefore they have never been in receipt of them within the meaning of section 40. But the present case shows the length to which it is sought by the Crown to push the alleged liabilities of a statutory agent under sections 43 and 42. Further, as regards super-tax on dividends, it may be pointed out that under the amended sections 57 and 58, the proper course is for the appropriate amount to be deducted by the principal officer of each Company concerned. This observation applies also to the dividends of the Bombay Company. It is true that the American Company is not a Company as defined by section 2 (6), and consequently must be assessed at an *ad valorem* rate and not at the flat rate of one anna payable by British Companies. But under the amended sections 57 and 58 the Income-tax Officer can call on the principal officer of the Company to deduct at the appropriate rate. So the exact rate should cause no difficulty. On the other hand the Bombay Company itself cannot be assessed for this deduction. Its principal officer is the person liable under sections 57 and 58. Nor in my judgment can the Bombay Company be made liable under sections 40 and 42, as I do not consider that it is in receipt of its dividends "on behalf of" its shareholders. Its duty is to pay these dividends, and not to receive them: and here I would respectfully follow the decision of Mr. Justice Greaves in *Imperial Tobacco Company of India Limited v. Secretary of State*, (1) which I have already dealt with in my judgment in the Hongkong Corporation case. As regards the actual assessments in the present case we have had them put in evidence by consent as Exhibits F and G together with the final notice of assessment of the 11th March 1927 Exhibit H which contains tabular statements clarifying the demands made upon the assessee.

12. On the basis then of the case before the Assistant Commissioner, I would hold that the questions submitted to us should in substance be answered in favour of the assessee and against the contentions of the Crown. Indeed apart from the questions of construction of sections 40, 42 and 43 dealt with in the Hongkong Corporation case, counsel for the Crown was prepared to concede that the assessments could not be supported except on a totally different ground which I will now deal with. This was that the Bombay Company was a sham Company, and a mere *alias* for the American Company, and that amongst other things the sale effected by the agreement Exhibit A was a fictitious transaction, and that in reality the American Company was carrying on its own business in the name of the Bombay Company, and that the Bombay Company was really a trustee of all its assets for the American Company. Counsel further claimed that these were findings of fact by the Commissioner, which were binding on us, and that on those findings the points of law submitted to us really did not arise or at any rate must be answered in favour of the Crown.

(1) 1 I.T.C. 169.

13. Turning to the case submitted to us, it will be found that para 2 is headed "Facts of the case," and then follow certain statements in paras 2, 3, 4 and 5. Para 6 purports to state the findings of the Income-tax Officer, and para 7 the findings of the Assistant Commissioner on appeal to him. Para 9 states the questions of law which the assessee wants to be decided, and then follows in paras 11 to 25 the opinion of the Commissioner as required by section 66 (2) of the Act.

14. Now undoubtedly in the opinion expressed by the Commissioner in paras 11 to 25, there are many statements made which if accurate would tend to bear out the contentions of Counsel for the Crown. But whether those statements can be supported in law having regard to the warning given by Lord Justice Younger in *Inland Revenue Commissioners v. Sansom*, (1) and to the general propositions of law which we referred to in *Commissioner of Income-tax, Bombay v. Sir Dinshaw Petit* (2) I very much doubt. But the opinion of the Commissioner however useful to us is not binding on us. It is the statement of facts in paras 2 to 8 with which we are more directly concerned. Now it would have been preferable if the Commissioner had stated specifically what facts were admitted or proved, as is usually done in cases stated by the Income-tax Commissioners in England. We have already objected in other cases to mere quotations of the submissions made by one side or the other. Any one party may submit anything. We want to have a definite finding whether that submission is correct having regard to the contentions of the other party.

15. Accordingly I would take exception to the manner in which para 4 is stated. This Court does not want allegations. And in any event it is no allegation of the assessee that "goods" are "sent to it for sale." This might imply that the goods were forwarded to it for sale as a commission agent, whereas the case for the assessee is that it buys outright in New York like other dealers, and that thereafter the American Company is not concerned in any way with the goods.

16. So, too, the statement in para 7 that the Assistant Commissioner was of opinion that "as a matter of fact the two (Companies) were identically the same" is inaccurate. The nearest approach to that statement is the following finding by the Assistant Commissioner, *viz.*, "It is hardly conceivable that there could be really a closer business connection than this between a non-resident and a resident. In fact they are hardly divisible, and the assessing officer as he has himself remarked could equally well have framed his assessment under section 42 (2)." The Assistant Commissioner was here discussing the applicability of section 43, and not whether the sale Exhibit A was fictitious.

17. Turning next to para 6, the Commissioner does not annex the original findings and order of the Income-tax Officer but says the latter found "that the whole of the Indian business in reality belonged to the New York Company," and that that Officer "took it that the purchase price at which the local companies were made to purchase the Remington goods from the New York Company was fictitious and not the actual cost to it." As the Commissioner has referred to this alleged finding of the Income-tax Officer, we thought it proper to call for it. This was objected to by the Crown but it was eventually

(1) 8 Tax Cas. 20; (1921) 2 K.B. 492.

(2) 2 I.T.C. 255.

produced by our directions, and on production the document in question showed that the Income-tax Officer arrived at no such finding. On the contrary he found that "these transactions appear perfectly straight-forward."

18. Indeed if the case for the Crown before the Income-tax Officer had been that the Bombay Company was a fictitious Company, and that the sales were all fictitious, that would surely have found a place in the appeal to the Assistant Commissioner. Further, it would seem certain that the Bombay Company would have raised a point of law for our decision as to whether there was evidence which would entitle the income-tax authorities in law to arrive at the conclusion that the agreement and transfers effected by Exhibit A were fictitious, and that the Bombay Company was a mere dummy.

19. As to how the Commissioner has been led into making these erroneous statements as to the findings of the Income-tax Officer and the Assistant Commissioner I do not know. But one difficulty they have caused me is in considering whether we ought under section 66 (4) to send the case back for restatement. In considering this I have also to consider the statement made by the Commissioner in para 5, *viz.* "All these purchase and sale agreements in reality appear to be mere paper transactions, the purchaser and seller being one and the same party, *viz.*, the New York Company which always was and continued to be the sole owner of the total Indian business whether under the style of the original Remington Typewriter Company (England) Limited or the All India Company or the three Companies in all in existence."

20. Now the case submitted to us has to be taken along with its Exhibits and annexures, and doing that I am unable to say under section 66 (4) that the statements in the case as a whole are insufficient to enable the Court to determine the questions submitted to it. The only real difficulty is caused by the Commissioner's allegations as to the Bombay Company being a fictitious Company. If once those allegations are put on one side, then though in certain particulars the facts might have been better stated they are sufficiently stated for us to dispose of the specific questions asked.

21. This leads one to the consideration of what is the position of the Commissioner when he states a case under section 66 (2). In the first instance it was urged strongly by counsel for the Crown that the facts of the case which are binding on this Court are those found by the Assistant Commissioner; that the Commissioner has no power to alter them apart from his power of review under section 33 which was not exercised in the present case; that the Commissioner was not hearing any appeal, and that consequently his functions were confined to stating a case as required by the assessee under section 66 (2), and therefore neither he nor the Court had any power to interfere with the findings of fact already arrived at by the Assistant Commissioner.

22. Thereupon counsel for the assessee pointed out that the findings of the Assistant Commissioner to which I have already alluded were all in favour of the assessee on this particular point and not against him. Finding on reference to Exhibit E that this was the fact, counsel for the Crown then proceeded to shift his position entirely, and to argue exactly the contrary to what he had previously urged as being the true construction of the Act and the true procedure. This further argument was to the effect that the Commissioner could state what he liked, and that whatever he stated we must accept as being the fact irrespective of the truth. Alternatively, counsel asked that the case should go back to the Commissioner, under section 66 (4) and that the

Commissioner might be at liberty to review the case under section 33, and thereby raise the point as to whether the Bombay Company was a fictitious Company.

23. I will say nothing as to the propriety of counsel for the Crown thus advancing two quite inconsistent arguments on the construction of a taxing Act and the proper procedure thereunder according as it might suit the exigencies of the particular case before the Court. But dealing with the alternative argument advanced, I think in law the Commissioner has no power to misstate a case as was the effect of the argument presented to us. His power and his duty is to state a case, and that means that he must state the relevant facts which have been proved or admitted before the Assistant Commissioner, apart from any limited right of appeal under section 32, or any review by the Commissioner himself under section 33, or to any rectification of a mistake under section 35.

24. Applying then that principle, I think that the Commissioner had no power to make the mis-statements which in the view I hold he did make. The Bombay Company was not charged before the Assistant Commissioner with being a fictitious Company and the transfer to it a sham. In the events which happened the case for both parties was closed at the termination of the proceedings before the Assistant Commissioner and it would be most unfair to allow the Commissioner to start an entirely new case against the Bombay Company without even giving it an opportunity of being heard on that point. Indeed even if he had exercised his powers of review—which in fact he did not do—it would have been obligatory on him under section 33 to give the assessee a reasonable opportunity of being heard. Apparently from para 13 of the reference the Commissioner was prepared to review the assessed quantum of manufacturer's profits *viz.*, 5 per cent, but he did not do so as this figure was not disputed by the Bombay Company. But he says nothing about reviewing the Assistant Commissioner's other findings, and admittedly there was no such review.

25. In the present case, therefore, I think we can see clearly what was the true position before the Assistant Commissioner, and that we can accordingly reject the additional and erroneous materials which the Commissioner has stated, and that there is no real necessity to send the case back to him for formal correction in this respect. I should have arrived at this conclusion irrespective of the judgment of the Income-tax Officer Exhibit XX which we admitted in evidence, for quite apart from Exhibit XX, I should clearly infer from the proceedings before the Assistant Commissioner that no such point could have been raised before the latter's subordinate officer. But out of abundant caution it seemed to me that we were entitled to look at this document seeing that the Commissioner himself had referred to it, and if one does look at it, then the inference I should otherwise have drawn is abundantly justified.

26. On the view then which I take of the case it is unnecessary to decide whether the Bombay Company was the agent of the American Company within the meaning of section 43 of the Act. But as the point has been argued before us, I would hold that it was such an agent. I need not repeat what was said by this Court in the Hongkong Corporation case as to the meaning to be attributed to the words "business connection" in section 43. But I am satisfied that in the present case the Bombay Company did have a business connection with the American Company within the meaning of that section. The

American Company was its vendor and promoter, and held substantially all its share capital. The Bombay Company traded in the machines of the American Company, and bought them from the American Company, and enjoyed the use of the trade name "Remington". Moreover, the purchase of the goodwill would prevent the American Company from canvassing the old customers within the area in question.

27. Accordingly I need not consider the precise meaning of the words in section 43 "through whom such person is in the receipt of profits." Here the American Company as shareholder was in receipt of the dividends paid by the Bombay Company, and the case therefore is somewhat stronger for the Crown than the Hongkong case where the relations between the parties were those of mere debtor and creditor.

28. As regards the request which is now made by Counsel for the Crown that the Commissioner should be given an opportunity of exercising his powers of review under section 33, our powers under this Act are limited, and holding, as we do, that we are in a position to decide the questions submitted to us without referring the case back under section 66 (4) we propose to answer them accordingly.

29. Turning to those questions, Nos. 1 and 2 seem to me to be too widely expressed for the necessities of the present case. I would accordingly answer them in a more limited way, as follows *viz.*, Questions 1 and 2. The Bombay Company, though an agent of the American Company within the meaning of section 43 of the Act, cannot be assessed to income-tax or super-tax under section 42 (1) of the Act or otherwise in respect of any profits made by the American Company on the sale of its goods to the Bombay Company inasmuch as the Bombay Company was not in receipt on behalf of the American Company of the profits in question, as is requisite under section 40. For similar reasons the Bombay Company is not liable to be assessed to super-tax upon dividends paid to the American Company by the Calcutta Company or the Madras Company: nor upon dividends on its own shares paid by it to the American Company. Super-tax upon dividends in the Bombay Company can be recovered by deduction by the Principal Officer of the Bombay Company under sections 57 and 58 of the Act.

Question 3. Yes.

30. As regards costs, I would direct that the costs of the Bombay Company be paid by the Commissioner to be taxed by the Taxing Officer, Original Side, as on the Original Side scale.

KEMP J.:—This is a reference under section 66 (2) of the Indian Income-tax Act XI of 1922 at the instance of the Remington Typewriter Company (Bombay) Limited, whom I shall call Remington (Bombay). The Commissioner regarded the facts as involving the interpretation of sections 42 (1) and 43 of the Act. The reference arises out of the assessment to income-tax and super-tax of Remington (Bombay) for the years 1925-26 and 1926-27 as agent of the Remington Typewriter Company of New York, whom I shall hereafter call the New York Company or Remington (New York).

It appears that the original Remington Typewriter Company was an English Company which sold its Indian business to the Remington Typewriter Company (India) Limited, a Company registered under the Indian Companies' Act, 1913, and having its register-

ed office at Calcutta. In his reference the Commissioner states that the Remington Typewriter Company (India) Limited came into existence in 1914 and allotted, as the purchase price to the English Company, 9,996 out of its 10,000 shares of Rs. 10 each to the New York Company as nominee of the English Company. The Indian Company carried on its business in India until the 12th of December 1921 when it sold its Bombay and Madras businesses to the New York Company which in its turn on the 18th of January 1922 sold the Bombay and Madras businesses to the Remington Typewriter (Bombay) Limited and the Remington Typewriter Company (Madras) Limited respectively. It thus appears that the Bombay business was done by Remington (Bombay), the Madras business by the Remington (Madras) and the business of the rest of India by Remington (India).

The reference relates to the assessment of the New York Company through its alleged agents Remington (Bombay) to income-tax and super-tax in respect of the dividends received by it through the three subsidiary Indian Companies and in respect of profits assessed at 5 per cent on the sales of Remington typewriters by the New York Company to the subsidiary companies. I refer to Remington (Bombay), Remington (Madras) and Remington (India) as the subsidiary Companies. Taking the agreement with Remington (Bombay) as typical of the agreement with Remington (Madras) whilst it appears that the goodwill of the New York Company in these Presidencies was sold to the respective subsidiary companies, there was, according to the assessee, no obligation on the New York Company not to supply Remington typewriters to other purchasers in those Presidencies. But however this may be, the practice was for Remington (Bombay) to purchase the typewriters from the New York Company at the usual wholesale price which was 40 per cent. below the catalogue price, Remington (Bombay) retaining any profit from sales within the territory within which it traded. It is only necessary to add that of the 60,000 shares of Rs. 10 each constituting the capital of Remington (Bombay) the New York Company under the agreement with it holds all the shares except three. One of these three shareholders is the Managing Director of all the three subsidiary Companies, another is alleged to be his Secretary and the third is the local Manager. Similarly with regard to the other subsidiary Companies the same three persons hold three shares only, the remaining shares in those Companies being held by the New York Company.

Remington (Bombay) has been taxed on all the dividends received by the New York Company and at 5 per cent fixed by the Income-tax Officer as the profit on sales to the subsidiary companies by the New York Company and not included in the profits shown by three subsidiary Companies. Remington (Bombay) appealed against the assessment to the Assistant Commissioner contending that there was no "business connection" between it and the New York Company and that it was not the New York Company's agent and it could not be taxed as such. The Assistant Commissioner dismissed the appeal. Remington (Bombay) then applied to the Commissioner under section 66 (2) to state a case for the opinion of the High Court. The Commissioner appears to have been of opinion on the facts that the New York Company and the Remington (Bombay) were identical. This was not the conclusion adopted by the Assistant Commissioner or the Income-tax Officer in proceeding under sections 42 (1) and 43 of the Act. They obviously treated the case as one in which Remington (Bombay) was the agent of the New York Company. Apparently

it was not present to the mind of the Commissioner that if Remington (Bombay) and the New York Company were identical the case would not be one under section 42 (1) and section 43 and in that view the questions submitted for our opinion would be merely a matter of academic interest and not questions arising on the facts as found by the Assistant Commissioner. But by accepting the position adopted by the Assistant Commissioner and referring questions under sections 42 (1) and 43 for our opinion, I take it that the Commissioner endorsed the Assistant Commissioner's view that the case was one which should be dealt with on the assumption that Remington (Bombay) was the agent of the New York Company and not the New York Company itself.

Now as I read section 40 of the Act, an agent in receipt of income on behalf of the non-resident can only be assessed in respect of such income as he receives on behalf of his principal. Therefore, in no case could Remington (Bombay) be treated under section 40 as assessee for the dividends received by the New York Company from the two other subsidiary Companies. Furthermore, in any event, although credit has been given in the assessments to super-tax for Rs. 50,000 on all the dividends received from the three subsidiary Companies, Remington (Bombay) claims—I think rightly—that if it is to be assessed for all the dividends of the three subsidiary Companies credit should be given for Rs. 50,000 in respect of the dividends from each of the three subsidiary Companies. The super-tax is on a sliding scale because by section 2 (6) of the Act the New York Company is a foreign company which has not obtained an order from the Central Board of Revenue under that clause. The flat rate of super-tax does not therefore apply to it.

But the relation between a Company and its shareholder is not a business connection under sections 42 (1) or 43 of the Act. Provision is made in the Act for deducting tax on dividends at the source. Furthermore, it was held by the majority of the Court in the case of *Imperial Tobacco Company of India Limited v. The Secretary of State for India*, (1) that the Company in that case could not be considered as an agent in receipt of dividends on behalf of one of its shareholders and with this opinion I respectfully agree. If the addition of the words "or through whom such persons.....or gains" in section 43 was intended to indicate the statutory agent as the source of the income to the non-resident that should have been clearly indicated. As to the dividends, therefore, I fail to see how Remington (Bombay) can be assessed under sections 42 (1) and 43 of the Act.

So far as sections 42 (1) and 43 are concerned it is necessary to decide first of all whether there is a "business connection" between the New York Company and Remington (Bombay). I am of opinion that in the ordinary meaning to be given to those words there is such a connection in this case. The New York Company owns all the shares in Remington (Bombay) except three and those are held by the Managing Director of all the three subsidiary Companies, his Secretary and the local Manager of Remington (Bombay). The position of the New York Company with regard to the other subsidiary Companies is similar. There is thus one control through one person as the Managing Director of all the subsidiary Companies. The New York Company own practically all the shares in the subsidiary Companies and the course of business has been for the New York Company to supply the typewriters at wholesale

prices to the subsidiary Companies; i.e., they have provided a market, by the creation of subsidiary companies for the sale of their typewriters. Such profits as the subsidiary Companies make on selling these typewriters locally come back to the New York Company in the form of dividends. The agreement between the New York Company and Remington (Bombay) is signed for both the vendors and the purchasers by the Managing Director Mr. Hull. I have no doubt in my mind that the circumstances here show a "business connection" between the New York Company and Remington (Bombay).

What then is the liability to tax of the assessee in respect of the income accruing due to the New York Company in British India? Under section 42 (1) profits or gains accruing to a non-resident from a business connection in British India are income arising in British India and the section goes on to state that in respect of them the "agent" is assessable. The argument turns round the question whether the agent here means an agent in receipt of the income on behalf of the non-resident as in section 40. It seems difficult to believe that whilst the Legislature intended that income accruing to a non-resident in British India should under section 40 render his agent in receipt of it on his behalf liable to be assessed in respect of it, it should at the same time provide another assessee who is the agent but not in receipt of the non-resident's income on his behalf, where such income consisted of the profits or gains through a business connection of the non-resident in British India. In both cases the income accrues in British India and it is difficult to see why the fact of a business connection should require a wider definition of agent. Mr. Taraporewala contends that there may be agents who are not in receipt of the income on behalf of the non-resident e.g., where the income from the business connection is remitted direct and the intention of the Legislature was to assess such an agent under section 42 (1) on behalf of a non-resident in respect of the profits or gains accruing through the business connection in India. Further that section 43 extends the meaning of such agents. In the alternative he suggests that if this be not so, but sections 40 and 43 must be read together then section 43 may not refer to the agent in section 42 (1) but to the agent in section 40 who is in receipt of income on the non-resident's behalf and, in any case, therefore, the agent mentioned in section 42 (1) need not be in receipt of the profits or gains on behalf of the non-resident. In other words sections 42 (1) and 43 should be read together but if sections 40 and 43 are to be read together, then section 42 (1) should be read by itself. The opinion of the majority of the learned Judges in *Imperial Tobacco Co. v. Secretary of State* (1) was to the effect that sections 40 and 43 should be read together.

I am of opinion that the agent mentioned in section 42 (1) must be intended to be the agent in receipt of income on behalf of the non-resident arising from the business connection. Such agent would be the person whom the Legislature would naturally regard as the assessee as the income would come to him on behalf of his principal. To hold otherwise would work an injustice because if he were an agent in the business connection on behalf of the non-resident and by the terms of his agency were not to receive the profits or gains arising from the business connection but they were to be received by somebody else, he would have no control whatever over the destination of such profits or gains and the proper person seems to be the person who is in the

proper legal possession as agent of such profits or gains. It seems to be the only way in which these three sections can be read consistently. Section 43 if covering the case of an agent who is not in receipt of the income on behalf of the non-resident would enable the Commissioner to treat as agent of the non-resident any subordinate employee of the non-resident who might have no control whatever over the income arising in British India. Before I am prepared to place such an interpretation on that section I wish to be satisfied in clear and unmistakable terms that such was the intention of the Legislature and in my opinion such a clear indication of its intention is not to be collected from the wording of those sections. Section 40 merely says income in British India of which the agent is in receipt on the non-resident's behalf renders the agent liable to assessment. Section 42 (1) states that profits and gains from the business connection are income accruing in British India. Therefore, if an agent of the non-resident is in receipt of it on his behalf such an agent is under section 40 assessable to tax in respect of it. Section 43 merely extends the meaning of the word agent without dispensing with the necessity of such statutory agent being in receipt of the income on the non-resident's behalf. Mr. Taraporewala for the Crown considers that every case referred to in section 43 is a case of a real agent. That may or may not be so. But it is noticeable that the section intends to designate as agents persons who might be such in law but would not in common parlance be known as such, as for example employees in the office. I am of opinion that sections 40 and 43 must be read together and that section 43, especially referring to the business connection mentioned in section 42 (1) inferentially gives to the meaning of "agent" in section 42 (1) an agent in receipt of income on behalf of the non-resident.

Whether the typewriters purchased by Remington (Bombay) are deliverable F.O.B. New York or not, I think that having regard to the business connection subsisting between the New York Company and Remington (Bombay) the profits and gains to the New York Company arise from this business connection. But I do not see how Remington (Bombay) could be regarded as the agent in receipt of profits and gains accruing from the business connection between the New York Company and the subsidiary Companies other than Remington (Bombay). It would be absurd to hold that the non-resident's agent in one business connection should be for that reason assessed as his agent in another business connection. The view that the agent must be in receipt of income on behalf of the non-resident from the business connection seems to me to receive support from the words "or through whom such person is in the receipt of any income, profits or gains" added in section 43 of the present Act. These words cover the case of an agent in section 42 (1) and cannot be read to create an inconsistency with the agent mentioned in that section.

It may be argued that the words in section 43 "through whom such person is in the receipt of any income, profits or gains" cover the case of profits received from the purchaser of goods who pays the price at New York but if this be so I think the Legislature should say so in clear terms and in my opinion the wording is very far from clear and should not, therefore, be so construed as to render a person not otherwise liable to be assessed subject to such a liability.

I agree, with respect, with the answers given by the learned Chief Justice to the questions submitted.

[247] IN THE HIGH COURT OF JUDICATURE AT MADRAS.

*Before Sir Murray Coutts Trotter, Kt., Chief Justice, Mr. Justice Ram-
sam, Mr. Justice Wallace, Mr. Justice Beasley and Mr. Justice Thiruvengkata
Achariyar.*

[20th March, 1928.]

A.L.S.P.L. Subramanian Chettiar and A.R.S.S.P.

Subramanian Chettiar

.. *Assesseees in Referred
Case No. 21 of 1926.*

A.L.S.P.P.L. Subramanian Chettiar, A.R.S.S.P.

Subramanian Chettiar and P.S.A.R. Lakshmanan

Chettiar

.. *Assesseees in Referred
Case No. 22 of 1926.**

v.

The Commissioner of Income-tax, Madras

.. *Referring Officer.*

*Income-tax Act (XI of 1922), Sec. 10 (2) (iii)—Loans by partner to
partnership beyond the initial subscribed capital—Stipulation in partnership deed
for interest thereon—Moneys borrowed used for capital expenditure—Interest
paid to lending partner—If deductible in the assessment of partnership profits.*

*Where a partner as such lends to the partnership beyond the initial sub-
scribed capital, sums of money under a clause in the partnership deed stipulating
for payment of interest thereon at an agreed rate and the sums so borrowed were
used for capital expenditure, the interest paid to him by the partnership must be
deducted under Sec. 10 (2) (iii) of the Income-tax Act in assessing the profits
of the partnership.*

Cases [Referred Cases Nos. 21 and 22 of 1926] stated under section 66
(3) of the Indian Income-tax Act, (XI of 1922) by the Commissioner of Income-
tax, Madras, for the opinion of the High Court in compliance with an order of
the High Court, dated 24-8-1926.

CASE. [R.C. 21 of 1926].

In pursuance of the order quoted above I have the honour to refer the
following case for the opinion of the High Court under section 66 (3) of the
Indian Income-tax Act, 1922.

2. The petitioners are Messrs. A.L.S.P.P.L. Subramanian Chettiar
and A.R.S.S.P. Subramanian Chettiar of Devakottai. From the year 1900,
they were carrying on money-lending business in partnership with others at
Tiruppur and Palladam, under the vilasam A.L.S.P.P.L. On 29th Chitrai
Sidharthi (12-5-1919) the partners other than the petitioners retired and the
business was continued by the petitioners jointly. The terms under which they
are carrying on the business in partnership are contained in a deed executed by
them on 29th July 1921. A translation of the deed is appended, Exhibit A.
According to the deed the share capital of the business is Rs. 21,000, of which
the senior partner A.L.S.P.P.L. Subramanian Chettiar has subscribed
Rs. 15,750 as his $\frac{3}{4}$ th share, and the other partner A.R.S.S.P. Subramanian
Chettiar has subscribed Rs. 5,250 as his $\frac{1}{4}$ th share; the profit or loss of the
business is to be enjoyed by them in proportion to their shares and on the amounts

*(1928) I.L.R. 51 Mad. 787; 55 M.L.J. 416; 28 L.W. 190; A.I.R. (1928) Mad. 889.

standing to the credit of each of the partners in the partnership accounts, interest at certain stipulated rates should be charged.

3. For the assessment of the year 1925-26 based on the accounts of 1924-25 the petitioners were called upon by the Income-tax Officer, Erode to make a return of their income under section 22 (2) of the Income-tax Act. They returned a profit of Rs. 26,166 from business. The Income-tax Officer called on them under section 23 (3) of the Act to adduce evidence in support of their return. They produced their accounts which were examined by the Income-tax Officer. The Income-tax Officer noticed that in arriving at the income shown in their return the petitioners had deducted certain inadmissible charges and the interest paid to the partners on their advances to the firm amounting to Rs. 40,835 as under:—

	Rs.
A.L.S.P.P.L. Subramanian Chettiar	40,757
A.R.S.S.P. Subramanian Chettiar	78

The Income-tax Officer found that the sums on which this interest was paid were advances of capital made by the partners for conducting and developing the business. He declined to admit the interest paid to the partners as a deduction from the profits of the firm on the ground that it represented a part of the profits of the partnership distributed to partners. He determined their total and taxable income to be Rs. 67,722 and charged income-tax and super-tax on this amount.

4. The petitioners appealed to the Assistant Commissioner and contended that a sum of Rs. 39,854 shown in the accounts as interest paid to the Madras shop of the senior partner A.L.S.P.P.L. Subramanian Chettiar should be allowed as a deduction in computing the profits of the partnership. The Assistant Commissioner called for and examined the accounts of the partnership. The sum of Rs. 4,01,251 standing to the credit of the Madras shop was made up thus:—

	Rs.
(1) By transfer from an old account of the business adjusted in 1919. This presumably represents previous years' profits	1,45,145
(2) By share of profit in No. 2 account of the business adjusted in 1921	84,680
(3) By share of profit in a partnership at Coimbatore adjusted in 1921	1,341
(4) By transfer from Thavanai account of A.R.S.S.P. Firm, Namakkal adjusted on 12—4—1924	73,890
(5) By interest on the above sums up to 12—4—1925	1,71,195
Total	<u>4,76,251</u>
Deduct amount transferred to current account in February 1924	75,000
Total	<u>4,01,251</u>

The bulk of the working capital of the partnership was put in by the partners. On the evidence before him, the Assistant Commissioner found that the subscribed capital of Rs. 21,000 was merely nominal, that there was an implied agreement between the partners, as suggested by the partnership deed that additional capital should be invested by the partners and that the large amounts which stood to the credit of the senior partner represented such advances of capital. In the light of this finding he was of opinion that the 'interest' paid to the partner, on these advances of capital was merely an assignment to him of a part of the net profits and that the provision in the partnership deed for such assignment made no difference to its character. He therefore upheld the Income-tax Officer's order disallowing the interest of Rs. 39,854 paid to the senior partner. He, however, made certain other allowances and reduced the taxable income of the firm to Rs. 66,001. A copy of his order is appended, Exhibit B.*

5. The petitioners then applied to the Commissioner under section 66 (2) of the Income-tax Act and required him to state a case to the High Court on the question of the admissibility of the interest paid to the senior partner as a deduction in computing the profits of the firm. My predecessor Mr. Strathie held the view that interest paid to a partner could be allowed as a deduction only when it was proved that the partner had made a *bona fide* legal loan to the firm and that the question whether there has been an advance of capital to a firm by one of its partners, or a *bona fide* borrowing of money by the firm from that partner was one of fact in each case. This view is supported by the decision of the Allahabad High Court in *In the matter of the Lala Mal Hardeo Das Cotton Spinning Mills* (1). It was also adopted by their Lordships the Chief Justice, Mr. Justice Krishnan and Mr. Justice Beasley in deciding three applications under section 66 (3) of the Income-tax Act last year. It was in view of this expression of opinion by their Lordships that Mr. Strathie, who had made a reference to the High Court (Referred Case No. 16 of 1925) on a similar question subsequently withdrew it with the consent of the party, M.A.R.N. Ramanathan Chetty, and by leave of the Court. In the present case Mr. Strathie agreed with the finding arrived at by the Assistant Commissioner on an examination of the partnership accounts that the sums advanced by the partner A.L.S.P.P.L. Subramanian Chettiar were advances of capital and, as he was of opinion that no question of law was involved, refused to state a case for the decision of the High Court. A copy of his order is appended, Exhibit C.*

6. On an application under section 66 (3) of the Income-tax Act I have been directed to refer the following question for the decision of the High Court.

"If a partner in addition to the subscribed capital lends to the partnership of which he is a member, a certain sum of money on the distinct understanding that in respect of this loan he is to receive interest from the partnership, whether or not the interest paid to the partner is a legitimate item of business expenditure within the meaning of section 10 (2) (iii) of the Indian Income-tax Act".

7. I should perhaps explain why such a question is raised and how it is of importance. The firm now assessed is an unregistered firm. Its partners

*Not printed.

(1) 1 I.T.C. 266.

therefore cannot get the benefit of section 48 of the Income-tax Act, *i.e.*, the assessment is not being made ultimately on them as individuals as it would be under the English Income-tax Law, but on the firm as such. The firm must pay the tax and the partner cannot get a rebate even though his personal rate of tax may be lower than that applicable to the income of the firm. Mr. A.L.S.P.P.L. Subramanian Chettiar suffered a loss in his business during the year of account. If the sum now in question *viz.*, Rs. 39,854 be eliminated from the firm's assessable income, the tax payable by the partnership in which he is a partner will be considerably reduced; he will not, however, pay tax in his individual assessment on the whole sum of Rs. 39,854 which he is said to have received as interest because a portion of this sum will have to be set off against his business losses *i.e.*, if this Rs. 39,854 is assessed in the hands of the firm the Crown will secure considerably more tax than would result from an assessment of the same sum as part of the income of the individual partner. This may appear inequitable, but it has to be remembered that members of unregistered firms enjoy certain advantages *e.g.*, a member of several unregistered firms "suffers" tax indirectly on his share of each firm's income only at the rates applicable to the income earned by such firms and not at the rate applicable to his individual total income (which includes his share of income of the various firms), though the latter rate may be higher. He may also benefit by the proviso to section 55 (as the senior partner of the firm in question has benefited in his individual assessment) under which if the firm has paid super-tax his share of its income is not taken into account in determining his individual income liable to super-tax. There is nothing whatever to prevent any firm from applying for and securing registration under section 2 (14) of the Income-tax Act and the rules framed thereunder, if, as in the present case, it is constituted under a partnership deed specifying the partners' shares. The fact that there are numerous unregistered firms indicates that if they lose in some ways they stand to gain in others and that the advantage of remaining unregistered appears to them to outweigh its disadvantages.

8. Regarding the form of the question before their Lordships I venture to submit that the use of the words "lends" and "loan" places me in a difficulty. I would answer the question as it stands in the affirmative, but would add that that answer cannot benefit the petitioners because in this case there has been no lending, but only the usual advance of capital by a partner. The petitioners' case appears to be based on the *maxim* that "a partner in a firm can have a dual capacity, that of a creditor of the firm as well as that of a partner in it". I do not wish to dispute the truth of this *maxim*. I agree that a partner may be invested with this "dual capacity" if, for instance, he has lent a definite sum of money to the firm on a formal document, or if the profits of the firm remain undistributed temporarily and if it is the practice of the firm to pay interest in such a case. But I emphatically deny that there are any circumstances in the present case to justify the view that the petitioner was a creditor to the firm in respect of the sum of Rs. 4,01,251 standing to his credit in the books, even though part of his profit from the partnership may have taken the shape of interest on this sum. The sum in question was not deposited temporarily for reasons unconnected with the business. It remained invested for about 6 years, obviously because the business required it, the subscribed capital of Rs. 21,000 being wholly insufficient. The fact that interest was charged on this "surplus capital" in the accounts is no proof that it was a loan. It is no uncommon thing

for a merchant trading on his own account, and not in partnership, to charge interest on his own invested capital as a business expense in the accounts, and to reckon as his business profit only the surplus remaining after this deduction has been made. The petitioners' manner of keeping their accounts is merely an adaptation of this practice to the requirements of a partnership.

9. My opinion therefore is that the petitioners are not entitled to a deduction of the interest paid to the partner on his advances of capital and that the question propounded by them does not arise out of the facts of the case.

EXHIBIT A.

Translation of Partnership Deed of Messrs. A. L. S. P. P. L. Subramanian Chettiar, Bankers, Tiruppur.

Partnership, dated 29th July 1921, between Messrs. A.L.S.P.P.L. Subramanian Chettiar and A.R.S.S.P. Subramanian Chettiar of Devakottai reciteth as follows:—

In the joint business started on 22nd Avani Sarvari (1900-1) between ourselves and some others at Tiruppur and at Palladam as a branch thereafter, under the Vilasam A.L.S.P.P.L. from 29th Chitrai Sidharthi onwards, we two carry on business in the said two places and under the same vilasam, with a share capital of Rs. 15,750, being $\frac{3}{4}$ th share of A.L.S.P.P.L. Subramanian Chettiar, and Rs. 5,250 being the $\frac{1}{4}$ th share of A.R.S.S.P. Subramanian Chettiar, totalling Rs. 21,000 being the share capital of the firm, we hereby agree after deducting expenditure to enjoy any profit or loss that may accrue, according to the proportion of shares held by us.

For the said business interest will be charged at the current rate charged by the Madras Chettis on their 6 months loans against amounts drawn on the 1st party's Madras shop Thavanai account, and on the amount standing in the name of his Devakottai shop current account, and for his Madras shop current account, at the rate charged by the Madras Chettis on their 6 months' Thavanai account, or in times of tightness or dullness as per letters of advice from Madras, and for the second partner's Namakkal shop Thavanai account and for his Devakottai shop current account at the rate charged by the Madras Chetti Pillais on their 6 months Thavanai account. As we have now been legally advised that a document should be drawn up with respect to the above partnership business, we hereby draw up this deed in accordance with the arrangements we have already arrived at between ourselves in our accounts.

CASE. [R.C. 22 of 1926.]

In pursuance of the order quoted above I have the honour to refer the following case to the High Court under section 66 (3) of the Income-tax Act, 1922.

2. The petitioners in this case are the firm of Messrs. A.L.S.P.P.L. Subramanian Chettiar, A.R.S.S.P. Subramanian Chettiar and P.S.A.R. Lakshmanan Chettiar. From the year 1902 petitioners Nos. 1 and 2 above were carrying on business in partnership with others at Gobichettipalayam and Bhavani under the vilasam "A.L.S.P.P.L." On the 26th Vaikasi Sidharthi (7th June 1919) the partners other than the first and second petitioners retired from the business. Thereafter these two persons admitted a third partner P.S.A.R. Lakshmanan Chettiar and are continuing the business in part-

nership. The terms under which they are said to have been carrying on the business are contained in a deed of partnership executed by them on 29th July, 1921. A translation of the partnership deed is appended, Exhibit A. According to the deed the share capital of the business is Rs. 20,100 of which the first partner A.L.S.P.P.L. Subramaniam Chettiar has subscribed Rs. 11,306-4-0 for his $9\frac{1}{16}$ share, the second partner A.R.S.S.P. Subramaniam Chettiar has subscribed Rs. 6,281-4-0 for his $5\frac{1}{16}$ share, and the third partner P.S.A.R. Lakshmanan Chettiar has subscribed Rs. 2,512-8-0 for his $1\frac{1}{8}$ share. The profit or loss of the business after deducting the expenses is said to be enjoyed by them in proportion to their shares. The deed further provides that on the amounts other than the share capital standing to the credit of the partners in the partnership accounts interest at certain fixed rates should be charged.

3. For the assessment of the year 1925-26 based on the accounts of the year 1924-25 the petitioners were called upon by the Income-tax Officer, Erode to make a return of their income. They returned a profit of Rs. 15,016 from business. The Income-tax Officer called on them to adduce evidence in support of their return. They produced their accounts which were examined by the Income-tax Officer. The Income-tax Officer noticed that in arriving at the income shown in their return the petitioners had deducted certain inadmissible charges and interest amounting to Rs. 23,471 paid to one of the partners A.L.S.P.P.L. Subramaniam Chettiar on his advances to the firm. He found that the sums on which this interest was paid were advances of capital made by the partner for conducting and developing the business. He declined to admit the interest so paid as a deduction from the profits of the firm on the ground that it represented a part of the profits of the firm distributed to one of its partners. After making certain other adjustments the Income-tax Officer determined the total and taxable income of the firm to be Rs. 43,342 and levied income-tax on this income.

4. The petitioners appealed to the Assistant Commissioner and contended that the sum of Rs. 23,471 paid to the partner A.L.S.P.P.L. Subramaniam Chettiar as interest on his advances to the firm should be allowed as a deduction in computing the taxable income of the firm. The Assistant Commissioner examined the accounts of the partnership from its inception i.e., from the year 1919. The sum standing to the credit of the partner A.L.S.P.P.L. Subramaniam Chettiar *viz.*, Rs. 2,36,242 was made up thus:

	Rs.
(1) By transfer from head-quarter account adjusted in April 1920. This presumably represents earlier profits ..	61,329
(2) By share of profits received on dissolution of a partnership conducted by the senior partner with two others in the years 1911-1914, adjusted in April 1922 ..	33,500
(3) By adjustment through the accounts of A.R.S.S.P. firm, Namakkal in June 1924 (as for April 1924) ..	67,418
(4) By interest on the above sums upto 12th April, 1925 ..	73,995
Total	<u>2,36,242</u>

On the evidence before him the Assistant Commissioner found that the subscribed capital of Rs. 20,100 was merely nominal, that there was an under-

standing between the partners as suggested by the partnership deed that additional capital should be invested in the partnership and that the amounts standing to the credit of the partner represented such advances of capital. In the light of this finding he was of opinion that the interest paid to the partner on the sums advanced by him as capital for the business was merely an assignment of part of the profits in his favour. In the result he agreed with the order of the Income-tax Officer in disallowing the payment of interest. A copy of his order is filed as Exhibit B.*

5. The petitioners then applied to my predecessor under section 66 (2) of the Income-tax Act and required him to state a case to the High Court on the question of the admissibility of interest paid to the partner as a deduction in computing the profits of the firm. He declined to state a case to the High Court on the ground that no question of law arose. A copy of his order is appended, Exhibit C.*

6. On an application made under section 66 (3) of the Income-tax Act I have been directed to refer the following question for the decision of the High Court:

"If a partner in addition to the subscribed capital lends to the partnership of which he is a member a certain sum of money on the distinct understanding that in respect of this loan he is to receive interest from the partnership, whether or not the interest paid to the partner is a legitimate item of business expenditure within the meaning of section 10 (2) (iii) of the Indian Income-tax Act".

7. I have been directed to refer the same question in the case of the A.L.S.P.P.L. Firm, Tiruppur, and for reasons analogous to those given in my reference in that case I am of opinion that the question does not arise on the facts of this case.

EXHIBIT A.

Translation of partnership deed.

Partnership deed, dated 29th July, 1921, executed by (1) Subramania Chettiar, son of A.L.S.P.P.L. Subramaniam Chettiar of Devakottai, (2) A.R.S.S.P. Subramaniam Chettiar, son of A.R.S.S.P. Sabapathi Chettiar and (3) Lakshmanan Chettiar, son of P.S.A.R. Shunmugam Chettiar of the same place reciteth as follows:—

In the joint business carried on from 8th Masi Pilava (1901-1902) by Nos. 1 and 2 above in partnership with some others at Gobichettipalayam in the Coimbatore district and then at Bhavani as its branch, under the vilasam A.L.S.P.P.L. from the 26th Vaikasi Sidharthi, we three carry on business at the said two places and under the same vilasam with a share capital of 9|16th *vis.*, Rs. 1,1306-4-0 for No. (1) A.L.S.P.P.L.'s share, 5|16th, *vis.*, Rs. 6,181-4-0 No. (2) A.R.S.S.P.'s share and 1|8th, *viz.*, Rs. 2,512-8-0 No. (3) P.S.A.R.L.'s share, totalling Rs. 20,100 being the capital of the firm, we hereby agree that after deducting expenditure to enjoy any profit or loss that may accrue according to the proportion of shares shown above. For the said business interest will be charged at the current rate charged by the Madras Chettis on their 6 months loans against amounts drawn from the 1st partner's Madras shop Thavanai account, and on the amount standing in the name of his Devakottai

*Not printed.

shop current account (Nadappu account)), and also on the amounts standing to the credit of the Madras current account, and in times of tightness at rates as per letters of advice from Madras and on the Thavanai account standing to the second partner's Namakkal shop and his Devakottai shop current account, at the current rate charged by Madras Chettis on 6 months Thavanai loans; and on the amounts standing in the current account of the third partner at the current rate charged by Madras Chettis on their six months Thavanai loans.

As we have now been legally advised that a document should be drawn up in respect of the above partnership business we hereby draw up this deed in accordance with the arrangements we have already arrived at between ourselves in our accounts.

K. S. Krishnaswamy Ayyangar and V. Rajagopala Aiyar, for Assesseees.
M. Patanjali Sastri, for Crown.

JUDGMENT.

RAMESAM, J.:—This case has been referred to us under section 66 (3) in pursuance of an order of this Court requiring the Commissioner of Income-tax to state a case and refer it.

The facts of the case are as follows:—According to a deed of partnership, dated 29th July 1921, Exhibit A, A.L.S.P.P.L. Subramanian Chettiar and A.R.S.S.P. Subramanian Chettiar entered into a partnership according to the terms of which the former contributed Rs. 15,750 as his $\frac{3}{4}$ share of the capital, and the latter contributed Rs. 5,250 being $\frac{1}{4}$ share of the capital, the initial capital agreed being Rs. 21,000 and they were to share the profit and loss in the ratio of 3 to 1. The document also contemplates that if necessary further sums may be contributed by either party towards the additional capital of the business and that interest should be charged on it. The Commissioner has found that the senior partner advanced a sum of Rs. 4,01,251 as additional capital in parts at various times and that the junior contributed comparatively a very small sum. The amount of interest on the senior partner's advances comes to Rs. 40,757 and the interest on the junior partner's advances to Rs. 78. It is now claimed on behalf of the partnership that the total of these two amounts of interest paid to the partners for sums advanced by them should be deducted in estimating the amount on which the partnership should be assessed for income-tax under section 10 (2) (iii). The Assistant Commissioner held that the whole of the additional sums advanced by the partners must be regarded really as the capital of the firm. On appeal the Commissioner in his order conceded that a partner may sometimes occupy a dual capacity, that is, he may lend a definite sum of money to the firm on a formal document in which case it would be regarded as a loan; but in the present case the sums advanced by the partners cannot be regarded as loans but as 'surplus capital'. The question to be decided by us is whether the sums advanced by the partners should be regarded as 'capital borrowed for the purpose of the business' within the meaning of section 10 (2) (iii). In the argument before us the learned Vakil who appeared for the Commissioner admitted that the sums advanced by the partners were capital, but he denied that it is capital "borrowed". The proposition of law for which he contended is that though a partner may make a loan to the partnership, he cannot lend capital to the partnership and that additional capital required for the purposes of the partnership can be borrowed only from outsiders; in other words, though capital may be borrowed from outsiders,

capital cannot be borrowed from a partner. He cited no authority for this proposition. The sub-clause itself does not contain any limitation as to the person from whom capital is to be borrowed. Once it is conceded that a partner can lend money just like any other third person it is difficult to see why he cannot lend capital also. Whether the money lent is capital or a mere loan really depends on the use to which it is put and not on the person from whom it was borrowed. If it is used for purposes similar to those for which initial capital is used, then it is capital in the hands of the partners by reason of the use which it is put to, though it was money borrowed from the partners. It is not the character of the lender that determines whether the sum borrowed is capital or not. The Commissioner seems to think that if a sum of money is deposited with the partnership temporarily for reasons unconnected with the business it is a loan, but if it is invested for a much longer time than the business required it, the initial capital being insufficient, then it becomes surplus capital and not a loan. We are not able to follow these distinctions of the Commissioner. All sums lent to the partnership are loans whoever the parties and whatever the purpose for which they are lent. After being borrowed if they are used like capital they become borrowed capital and if they are not so used they continue to be mere loans, the expenditure not being in the nature of capital expenditure (Vide clause 9 of the same sub-section). In the present case the Commissioner himself found that it was capital and there is no doubt also that it was borrowed from the partners. That being so, we are of opinion that section 10 (2) (iii) applies.

It is said that there is a finding of fact by the Commissioner that the sums in question in this case are not capital borrowed within the meaning of the clause in question. The so-called finding of fact is really based upon certain facts pure and simple as to which there is no dispute and which are accepted on all hands *plus* certain supposed legal principles on which the Commissioner relies but for which there is really no authority. Wherever a sum is borrowed and it is afterwards used for capital expenditure it is not open to the Commissioner to find that it is not borrowed capital as there is no such principle of law as is contended before us on behalf of the Commissioner. It is also said that there is a finding that the initial capital was nominal and from the beginning additional capital was intended. Here again there is no dispute about the facts. The initial capital consisting of two amounts which the parties were bound to contribute, is known. So far as additional or surplus capital is concerned no partner is bound to advance any particular sum. All that the deed provides is that if a partner chooses to advance certain sums he will be entitled to interest, but he is not compellable to do so. It is clear therefore that what is called surplus capital has different characteristics from the initial capital and it is not open to ignore this difference. The fact that a large business was contemplated for which the small initial capital would not be enough and additional capital would therefore be required has really no bearing on the legal aspect of the question, additional capital having different incidents from initial capital. Moreover, however high may be the proportion one partner may contribute in the form of additional capital relatively to the other partner, it will have no bearing on the proportion in which the profits are to be taken. This again shows that it is not open to regard additional capital as really initial capital. The Commissioner's findings being based on misconceptions of law cannot be accepted as findings of fact binding upon us.

The only other question is whether interest paid on the sums advanced can be said to be in any way dependent on the earning of profits. It is clear that the clause "Where the payment of interest thereon is not in any way dependent on the earning of profits." relates to the pavability of interest, that is, the clause excludes cases where interest is payable in some manner dependent on the earning of profits. If interest is payable whether profits are earned or not, the clause applies. The learned Vakil for the Commissioner argued that the scheme of the Act showed that wherever profits are earned, they were intended to be wholly assessed and the construction we are placing on this clause is inconsistent with the scheme of the Act. There is no such general scheme in the Act. In this respect the law in India seems to be different from that in England and the English cases mentioned by the learned Vakil for the Commissioner have really no bearing on the construction of the Indian Act and need not be referred to. It is hardly necessary to observe that, when interest is deducted from the earnings under this clause by the partnership as its expenditure, it is really profit earned by the individual partner who takes the interest and it will be added to his income in assessing him individually. The actual rate of assessment and to what extent the State is profited or loses by the change in the assessee depends really on the actual income of the individual partner for the particular year and in the case where he has lost in his trade in any year the transfer of the amount as his income may merely reduce his losses and may not result in any assessment. But these are all accidental circumstances which may vary year after year. One year the State may lose and another year the partnership may lose. Gain or loss to the State is really irrelevant for our purpose.

There is one further observation to be made. It is only where interest is paid that the deduction contemplated by section 10 (2) (iii) is permissible. Payment need not be actually in cash, but may be by adjustment of accounts; but in whatever manner it is done it must be a real out-going. In the present case the Commissioner has found that interest has been paid as the question referred to us shows. There may be cases where no interest has yet been paid, but may be due only. In such a case the partnership cannot ask for deduction of the interest merely on the ground that it is due. Therefore no question arises before us on this aspect of the matter.

We therefore answer the question referred to us as follows:—

Where a partner as partner lends money beyond the initial capital to the partnership at an agreed rate of interest and the money is used for capital expenditure, the interest paid by the partnership to him in the year of assessment must be deducted in computing the profits or gains of the partnership within the meaning of section 10 (2) (iii).

Costs Rs. 500 will be paid by the Commissioner of Income-tax to the assessee.

THE CHIEF JUSTICE:—The above judgment represents the joint view of Ramesam, J., and myself and was drafted by him after full discussion between us.

Referred Case No. 22 of 1926.

This is governed by our opinion in the other case.

Costs Rs. 100 will be paid by the Commissioner of Income-tax to the assessee.

WALLACE, J.—I agree with the statement of the law applicable to this case as expounded by my learned brothers, the case being one where, on the facts found, there was a genuine borrowing of capital at the prevailing market rate of interest. I only wish to guard myself against the supposition that in other cases it will not fall to be decided as a point of fact whether the alleged borrowing of capital was not a genuine loan, but a mere device to evade the Act. To take an extreme case:—Where two partners agree on a nominal capital and then each lends additional capital at a fancy rate of interest calculated so high or with so little relation to the market rate, as to be obviously designed to absorb all probable profits, and thus enable them to submit a nil profits return, it would surely be open to the Commissioner to find that there was no genuine borrowing of capital. I agree that the present case falls under section 10 (2) (iii) of the Indian Income-tax Act.

BEASLEY, J.—I agree and make the same reservation as Wallace, J.

THIRUVENKATACHARIAR, J.—The answer to the question referred to the Full Bench depends upon the meaning which should be ascribed to the expression “capital borrowed for the purposes of the business” in section 10. Cl. (2) (iii) of the Indian Income-tax Act. It was argued by the learned Vakil for the Commissioner that any sum of money which a partner puts into the business of a firm for being used as capital cannot be treated as a loan from him to the partnership, even though the firm purports to borrow the amount from him as a loan: in other words a firm cannot legally borrow its capital from its partners. This proposition would be quite correct if by ‘capital’ is meant the sum which a partner contributes under the agreement of partnership for the purpose of commencing or carrying on the business and which is intended to be risked by him in the business. That is the true sense of the word “capital” and so far as the contributions made by a partner relate only to capital so understood, he is not a creditor of the firm. He has no right to sue the firm for the recovery of such contributions or advances and he can only get back his capital on the dissolution of the firm, out of any surplus assets which may remain after meeting all its liabilities. But in the clause we have to construe, the word “capital” appears to be used not in the sense of a partner’s contribution as capital which as pointed out cannot be treated as borrowed capital but as meaning sums borrowed for capital expenditure. Such a borrowing by a firm whether from an outsider or from one of its partners cannot have the effect of increasing the capital of the firm. As observed in Lindley on Partnership: “If a firm borrows money so as to be itself liable for it to the lender, the capital of the firm is no more increased than is the capital of an ordinary individual increased by his getting into debt”. So it is the advances made by a partner to a firm over and above the amount which he has agreed to subscribe towards the capital of that business, cannot be treated as an increase of his capital, but as a loan made by him and if such advances are made for being used for the same purposes for which the original capital was intended to be used, they will be capital borrowed for the purpose of business within the meaning of section 10, clause (2) (iii) and if the other requirements of that clause are satisfied the payment of interest on such borrowings should be deducted from the profits of the business. It is a question of fact in each case whether the further advance made by a partner over and above the capital agreed to be put in by him is really a loan by him to the partnership, or an increase of his capital in the business made with the consent of the other partners. So far as the present

case is concerned the question referred treats the advances in question as loans made by the partner to the firm for being utilised as capital and there seems to be no valid ground for questioning that fact. I therefore agree that the question should be answered in the affirmative.

[248] IN THE HIGH COURT OF JUDICATURE AT CALCUTTA.

Before Sir George Rankin, Kt., Chief Justice, Mr. Justice C. C. Ghose and Mr. Justice Buckland.

[26th March, 1928.]

Messrs. Harmukhrai Dulichand

.. *Assessee.**

v.

The Commissioner of Income-tax, Bengal

.. *Referring Officer.*

Income-tax Act (XI of 1922), Secs. 22 (2), (4), 23 (3) and (4)—Assessee sending a return of income—Subsequent issue of a combined notice under Secs. 22 (4) and 23 (2) to produce accounts and evidence—Accounts not produced, but evidence tendered—Issue of a combined notice, if valid—Assessment under Sec. 23 (4), if legal.

A combined notice issued in one Form headed as under Secs. 22 (4) and 23 (2) of the Income-tax Act is not illegal or void.

Where an assessee after submission of return in compliance with a notice under Sec. 22 (2) was served with a notice in a combined Form under Secs. 22 (4) and 23 (2) and while complying with the notice under Sec. 23 (2) by producing the evidence, has failed to comply with the terms of the notice under Sec. 22 (4), the Income-tax Officer is entitled to make an assessment under Sec. 23 (4) for failure to comply with the notice under Sec. 22 (4) and is not bound to proceed under Sec. 22 (3) of the Act.

Chandra Sen Jaini v. Commissioner of Income-tax, United Provinces, 3 I.T.C. 17, Followed.

Brijraj Rangalal v. Commissioner of Income-tax, Behar and Orissa, 2 I.T.C. 458, Dissented from.

Case stated under section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bengal, for the opinion of the High Court.

CASE.

At the request of Messrs. Harmukhrai Dulichand and under the provisions of section 66 (2) of the Indian Income-tax Act (XI of 1922) I have the honour to refer to the Hon'ble High Court two questions of law, hereinafter stated, arising out of the assessment of the above firm to income-tax for the year 1926-27.

2. The facts of the case are as follows:—

Messrs. Harmukhrai Dulichand, hereafter called "the Assessee," an unregistered firm, having their offices in Calcutta, are commission agents and wholesale dealers in piece-goods, keeping the Dewali year ending in October as their year of account. On the 5th of May 1926 a notice was issued upon

them by the Income-tax Officer, District I (1) Calcutta, calling for a return of their income during the previous year, *viz.*, Dewali 1981-82. A reminder for the submission of the return was issued on the 6th July. No return having been received, on the 22nd July the Income-tax Officer issued a notice under section 22 (4) calling for accounts of the year 1981-82 (Dewali), being the previous year upon the basis of the profits of which the assessment of 1926-27 was due to be made and also of the year 1980-81 (Dewali). On the 4th August the assessee submitted their return showing a loss of Rs. 26,000. Thereupon, on the 19th August, the Income-tax Officer issued a notice under section 22 (4), calling for accounts of 1980-81 and 1981-82 combining in the same notice a notice under section 23 (2) requiring the assessee to produce any other evidence (*i.e.*, besides the account books of 1980-81 and 1981-82 called for under section 22 (4)) upon which they relied in support of their return. The notice was worded as follows:—

“Notice under section 23, sub-section (2), and section 22, sub-section (4) of the Indian Income-tax Act, XI of 1922, (for use when a return has been made).

Messrs. Harmukhrai Dulichand.

To enable me to test the correctness of the return of your income furnished by you under section 22 (sub-section 2) of the Act for the year Dewali 1981-82, I hereby require you to produce or cause to be produced at the place and time mentioned below the accounts and documents specified overleaf (the accounts of 1980-81 and 1981-82 Dewali were specified overleaf) and any other evidence on which you may rely in support of your return.”

On 14th September, 1926, the assessee by their pleader appeared before the Income-tax Officer, and representing that the accounts of 1980-81 had been sent to Bikaner owing to the Calcutta riots, prayed for time to produce them. This was allowed. On the 17th November, 1926, a partner of the firm appeared before the Income-tax Officer and stated that the 1980-81 accounts were on their way. A prayer was made for 2 days' time. The case was thereupon adjourned to 23rd November, 1926. On this date the assessee's pleader appeared before the Income-tax Officer and asked for a further one day's time, on the ground that his clients, the assessee, had failed to appear. This prayer was allowed. The books of 1981-82 were examined on various dates after this and on 26th February, 1927 the assessment was made. The books of 1980-81 were not produced. During the examination of the books of the previous year produced, *viz.*, 1981-82 difficulties arose regarding the valuation of stocks. Stocks had been valued in the accounts but, in addition, there were items of losses calculated on account of fall in the price of goods not yet sold. Inspection of the books of the year anterior to the previous year was therefore necessary in order to check the value of the stocks, especially in view of the fact that books had not been produced in connection with last year's assessment (*viz.*, 1925-26), and to ascertain the regular method pursued by the assessee in valuing stocks. As the books of 1980-81 were not produced assessment was made for that default under section 23 (4). A copy of the assessment note is annexed for the information of the Hon'ble Judges.

The assessee presented a petition under section 27 of the Act denying that they had been guilty of negligence, in that, the books of 1980-81 having been sent to Bikaner they were unable to produce the same within the period

allowed. The Income-tax Officer rejected the petition, holding that sufficient time had been granted. The Assistant Commissioner upheld this decision on appeal.

3. It is obvious from the above account that the assessee made no effort to produce the books of the year 1980-81. Beyond mere statements that the books had been sent to Bikaner they gave no reasons and produced no evidence to show why the books could not be produced. Had the books been really sent to Bikaner they were granted ample time to produce them. The requisition under section 22 (4) was issued on 19th August 1926. The assessment was not completed till 26th February 1927. The intervening period was obviously more than ample to enable the assessee to send for the books from Bikaner and produce them in Calcutta. I therefore hold as fact that the assessee wilfully failed to produce their books of 1980-81. I also hold that the books were rightly requisitioned under section 22 (4), being necessary in purpose, in particular, of verification of the figures of stock contained in the books of the previous year and for the purpose of ascertaining what was the regular method employed by the assessee in valuing their stocks.

4. The assessee now contend:—(a) that a notice under section 22 (4), being combined with a notice under section 23 (2) in one form of notice, was not in proper form and therefore not a legal notice, (b) that a notice under section 22 (4) cannot issue after a return has been made, but a return having been made, the only course open to the Income-tax Officer is to proceed under sections 23 (2) and 23 (3).

5. The following two points of law are therefore referred to the Hon'ble High Court:—(a) Was the notice under section 22 (4), which issued in this case so defective as to be legally null and void? (b) If an assessee has made a return in compliance with a notice under section 22 (2) and thereafter a notice has been served upon him under section 23 (2) and also a notice under section 22 (4), and the assessee has complied with the terms of the notice under section 23 (2) by producing the evidence upon which he relies, but has failed to comply with the notice under section 22 (4), is the Income-tax Officer entitled to make an assessment under section 23 (4), for failure to comply with the notice under section 22 (4), or is he bound to proceed under section 23 (3)?

6. I am required by the Act to state my opinion, which is as follows:—

In regard to question (a) the assessee have adduced no reason why the notice should be regarded as defective, beyond the fact that notices under two sections were combined in the one notice. The notice was headed "Notice under sections 23 (2) and 22 (4)" and called for certain specified account books under the latter section and under the former section for any other evidence upon which the assessee might rely in support of their return. There appears to be no defect in point of form in this notice. The Act does not require that the notices should be issued in any particular form to be prescribed by rules under section 59 and it appears to be open to the Income-tax Officer to issue such notices in any form that he chooses or that may be prescribed (as the form actually used was prescribed) by executive order so long as the requirements of the notices are those specified in the sections. There appears to be no reason why the requirements of two different sections should not be combined as a mere matter of convenience in a single notice as has been done. Moreover the assessee were not in any way prejudiced by the form of the

notice, but understood clearly what was required of them. Again they raised no objection on this score at the time when the assessment was being made. On the contrary, by applying for time to produce the 1980-81 accounts, they accepted the notice calling for them as legal and valid. My opinion, therefore, is that the notice was a legal and binding notice and that question (a) should be answered in the negative.

7. In regard to question (b), the assessee's contention is that, once a return has been filed, section 22 (4) ceases to be applicable and assessment must be made after issue of notice under section 23 (2) according to the provisions of section 23 (3) so that the powers of an Income-tax Officer are limited to consideration of the evidence produced by the assessee and such other evidence as the Income-tax Officer may require on specified points. In support of this interpretation of the relevant sections of the Act the assessee relies upon the words in section 23 (4) "or, having made a return." Their contention is in fact that section 23, sub-section (4) is divided into two parts, the first stating what may be done before a return has been filed and the second what may be done after a return has been filed.

8. I submit that this contention is not justified by the rules either of grammar or of legal interpretation, by practical considerations, or by what can be gleaned from other sources if I may be permitted to refer to them as to the intentions of the Legislature. In order that the sub-section might bear the meaning that the assessee seeks to place upon it, it would be necessary to insert the words "having so failed to make a return" before the words "fails to comply with all the terms of a notice issued under sub-section (4) of the same section." As the sub-section stands it contemplates three distinct cases:— (1) Failure to make a return, (2) Failure to comply with a notice under section 22 (4), and (3) Failure to comply with a notice under section 23 (2). By no twisting of language, I submit, can the second case be subsumed under the first case or made dependent on it. The three cases are absolutely independent. The words "having made a return" are clearly intended to emphasize *pro major cautela* the fact that even though a return has been made, failure to comply with a notice under section 23 (2) still deprives the assessee of his right of appeal. Or if it be contended that they imply an antithesis to what has preceded, the antithesis is surely between a default under section 22 (4), which may occur whether an assessee has made a return or not, and a default under section 23 (2) which can only occur when he has made a return. Logically this antithesis is as satisfactory as that suggested by the assessee, while, unlike the latter it is consistent with section 22 (4) and the general scheme of the sections. It is therefore preferable. If this explanation be considered unconvincing, the fact still remains that the words "having made a return" merely state what is actually true, namely, that a notice under section 23 (2) can only be issued after a return has been made. Even if it be necessary to regard them as mere surplusage, I submit that there is more justification for so regarding them than for reading the preceding part of the sub-section as though it contained the words "having so failed to make a return" which it does not contain, and absolutely no more justification (to say the least) for reading the words "having so failed to make a return" into the section than for reading the words "whether he has made a return or not" into it. Moreover section 22 (4) itself clearly indicates the only restriction placed on the power of the Income-tax Officer to issue a notice under that sub-section, namely, that a

notice calling for a return must have been issued. It is surely reasonable to suppose that if the Legislature had intended to impose any other restriction, they would have specified it in section 22 (4) along with the restriction already specified there and would not have introduced it casually in section 23 (4) which is not the place for it.

9. The scheme of the sections, I submit, is quite clear. Section 22 (4) gives the *Income-tax Officer* power to call for such evidence as he requires. Section 23 (2) requires him, when a return has been made to give the *assessee* an opportunity of producing such evidence as *he* wishes to adduce in support of his return. If section 23 (2) did not exist, it would be unfair to the assessee. If section 22 (4) did not exist, the task imposed on the Income-tax Officer would become extremely difficult if not impossible. On common sense or practical grounds I submit that there could be no justification for depriving the Income-tax Officer of the power to call for evidence from the moment that a return has been filed. The report of the All-India Income-tax Committee of 1922, which considered the bill which ultimately became Act XI of 1922, clearly shows what was intended. It says (paragraph 34) "We agree.....that a Collector" (now Income-tax Officer) "should have power to call for the production of accounts whether a return has or has not been filed." Again, the statement of objects and reasons says (paragraph 14) "The bill provides that the assessor" (now Income-tax Officer) may call for accounts whenever he considers it necessary." I submit that the Legislature has given effect to this intention without any ambiguity.

10. It seems evident that the aim of the Legislature was to secure that as far as possible assessments should be based on proper materials, such as accounts. As already stated they gave the Income-tax Officer power to call for such evidence as he might require and the assessee having made a return an opportunity to substantiate his return.

Under section 37 they gave the Income-tax Officer the powers of a Civil Court in regard to the issue of summons requiring the attendance of persons or the production of documents. Having regard to the powers conferred on Income-tax Officers, where assessee themselves are concerned, by sections 22 (4) and 23 (2) it is evident that the powers conferred by section 37 are mainly required to secure the attendance of, or production of documents by, persons other than assessee.

In section 23 (3) there is a reference to "such other evidence as the Income-tax Officer may require on specified points." The meaning of this is somewhat doubtful, except in so far as it obviously refers to further evidence required to elucidate or supplement evidence already produced by the assessee, whether in response to a notice under section 22 (4), or in response to one under section 23 (2). It has been doubted whether the words confer a specific additional power to call for further evidence upon the Income-tax Officer, or merely refer to powers that he possesses under the sections already mentioned.

The latter interpretation seems probable, because failure to comply with a requisition for evidence on specified points under section 23 (3) is not mentioned in section 23 (4) as one of the forms of default that deprive an assessee of his right of appeal.

11. If the assessee fails to produce evidence called for by the Income-tax Officer under section 22 (4) or section 23 (2) and also if he fails to make

a return the assessment still has to be made, but the Income-tax Officer, in the absence of proper materials, has to make it "to the best of his judgment." Where this is done, the assessee has no right of appeal. The forfeiture of the right of appeal is not merely a recognition of the hard fact that an assessee who will not furnish materials for an assessment can hardly have materials on which to base an appeal that would merit serious consideration, but was also intended to offer assesseees a substantial inducement to produce accounts and other evidence so as to enable Income-tax Officers to make accurate assessments, thereby doing justice alike to the individual assessee and to the 'Revenue', that is, to the general body of tax-payers.

Of course, even if a man produces such accounts as he has and complies with all notices issued to him, there may not be satisfactory materials for an accurate assessment, and the Income-tax Officer may still be compelled, in order to perform his statutory duty of making an assessment, to proceed upon an estimate. In such a case the assessee is not deprived of his right of appeal, but in the nature of the case, for reasons just given, it is, as a rule, of little practical benefit to him.

12. The practical result of the interpretation of the law put forward by the assesseees in this case would be to throw the whole of this machinery out of gear.

An assessee, according to this interpretation, could deny the Income-tax Officer access to his accounts provided that he had made a return, which he may do at any time before the assessment is made unless the Income-tax Officer had recourse to the issue of a summons under section 37. If a summons is issued under section 37 and the assessee disobeys it, whatever other penalties he may incur he does not forfeit his appeal against the assessment. So soon as a return of income under section 22 has been made the Income-tax Officer is deprived of his powers under section 22 (4).

Under section 23 (2) the assessee is to produce the evidence upon which he may rely. He has full discretion as to what he should produce. So long as he produces anything at the time and place prescribed in the notice under section 23 (2) he has not made a default under that sub-section.

Failure to produce evidence on specified points under section 23 (3), (if it be assumed that a specific additional power to call for evidence is conferred by that sub-section) does not entail forfeiture of the right of appeal.

Except, therefore, by invoking section 37—which was evidently not intended to be used for such a purpose, though no doubt it could legally be so used—an assessee, provided that he has put in a return of his income, cannot, according to this doctrine, be compelled to produce the evidence—accounts, etc., in the absence of which a proper assessment cannot be made but his refusal to produce such evidence does not deprive him of his appeal.

13. What the Act evidently contemplates is that assessments should be made after the Income-tax Officer has had an opportunity of considering all the relevant evidence. Most of that evidence is necessarily accessible to the assessee and to no one else and the Legislature intended that failure to produce it should entail forfeiture of the right of appeal. The interpretation that the assesseees seek to place upon these sections clearly runs counter to, and to a considerable extent would defeat, that intention, and would go far to render section 22 (4) *otiose*.

It involves consequences that I submit the Legislature can clearly not have intended.

In conclusion I may quote in support of the contention that I have put forward (that a notice under section 22 (4) may be issued even after a return has been made), the following sentence from the Judgment of Mr. Justice Mukherjee in the case of *Nirmal Kumar Singh Nowlaksha v. Secretary of State for India in Council* (1) delivered in this Court on January 26th, 1925:—
"When a return is submitted under that section" (i.e., section 22) "the Income-tax Officer may proceed to deal with the matter on the basis of the return and may not require the assessee to produce any further material, or he may, as required by sub-section (4) of that section, call upon him to produce or cause to be produced such accounts or documents as the Income-tax Officer may require."

14. My opinion in regard to question (b) therefore is that in the circumstances stated in the question the assessment may be made under section 23 (4).

N. N. Sircar and Amulya Chandra Sen, for the Assesseees.

B. L. Mitter (Advocate-General) and S. M. Bose, for the Crown.

JUDGMENT.

RANKIN, C. J.:—In this case the Commissioner of Income-tax has referred two points of law to this Court for its opinion under section 66 of the Indian Income-tax Act (XI of 1922). Before setting out the form of the questions it may be as well to premise that the assesseees in this case are a firm called Messrs. Harmukhrai Dulichand.

It appears that on the 4th of May, 1926, an ordinary notice was served upon them under clause (2) of section 22 requiring them to render a return of their income for the purpose of income-tax. It appears that the year by which this firm goes in maintaining its books of account is the *Dewali* year and the year of assessment was 1982-83, the previous year or the year of accounting being, therefore, 1981-82. On the 22nd of July, 1926, a notice under section 22 (4) was served upon them asking that they should produce their books of account for the *Dewali* years 1980-81 and 1981-82 and on the 6th of August 1926 the assesseees submitted a return. The return which they submitted consists of the words and figures "Loss Rs. 26,000" under the head "business". A notice was then issued upon them being a combined notice purporting to be under clause (2) of section 23 and also clause (4) of section 22. That required them to produce the accounts for 1980-81 and 1981-82 and also gave them an opportunity to call any other evidence on which they might rely in support of their return. On the date fixed by the notice the books of 1981-82 were examined and various adjournments were taken for the production of the books of 1980-81. There was a hearing, on appointment, on the 26th August, 1926, on the 10th of January, 1927, and on the 16th of February, 1927, and the final order of assessment was not made till the 26th of February, 1927. Although, therefore, these books for 1980-81 were called for, at all events, on the 6th of August, 1926, they were not produced by the following February at the time when the assessment was made. The Income-tax authorities have held that ample time was given for their production and that their non-production was wilful, as indeed

it is reasonably obvious from the dates and also from the inconsistent stories told by these assesseees to the effect that their books for the year in question were sent to Bikaner, because of the Calcutta riots and also, because of settling some disputes. The finding of fact is that these accounts are still deliberately withheld. There can be no question that for the purpose of finding what was the profit or loss for the year 1981-82 it is necessary to get the books of the year previous to that, because on any question of loss caused by fall in the value of stocks it is most necessary to see on what basis the valuation has been taken. The result, therefore, was that the assesseees had deliberately withheld the best evidence—indeed the only evidence that would enable one to test the accuracy of the return.

It is in these circumstances that the assesseees having failed before the Income-tax authorities requested that two points of law should be referred to this High Court by the Commissioner of Income-tax. The first question is: "Was the notice under section 22 (4) which was issued in this case so defective as to be legally null and void?" The second question is this: "If an assessee has made a return in compliance with a notice under section 22 (2) and thereafter a notice has been served upon him under section 23 (2) and also a notice under section 22 (4), and the assessee has complied with the terms of the notice under section 23 (2) by producing the evidence upon which he relies, but has failed to comply with the notice under section 22 (4), is the Income-tax Officer entitled to make an assessment under section 23 (4), for failure to comply with the notice under section 22 (4), or is he bound to proceed under section 23 (3)?" In my opinion both of these questions must be answered against the assesseees.

The first question is whether there is anything illegal in the issue of a notice under section 23 (2) and section 22 (4). I am of opinion that there is no reason why these two notices should not be comprised in one document. The position is that the assessee is given one date on which he is first of all to produce certain accounts or documents required by the Income-tax Officer and he is also told that on that same date he will get an opportunity of producing any further evidence upon which he relies. I can see no objection at all to that procedure and I observe that in the case cited to us from the Allahabad High Court decided on the 4th of January of this year *Chandra Sen Jaini v. Commissioner of Income-tax, United Provinces*(1) a Division Bench of that Court was of the same opinion. In my judgment there is no difficulty upon the answer to the first question.

The second question depends upon the construction to be put upon the 22nd and the 23rd sections of the Income-tax Act. By section 22 provision is made to the effect in the case of companies that the principal officer shall before the fifteenth of June in each year furnish a return of income without being asked. Provision is also made in the case of other persons whose total income is in the Income-tax Officer's opinion such as to render such persons liable to income-tax, that the Income-tax Officer may serve a notice requiring a return to be made. The concluding paragraph of that section then provides that the Income-tax Officer may serve on the principal officer of any company or on any person upon whom a notice has been served under sub-section (2), a notice requiring him, on a date to be therein specified, to produce, or cause to be produced, such accounts or documents as the Income-tax Officer may require, pro-

vided that he shall not require the production of any accounts relating to a period more than three years prior to the previous year. That provision which enables the Income-tax Officer to require the production of accounts or documents is in the case of persons other than companies a power given on condition that a notice has been served requiring the making of a return. There is no sign in that clause of any further condition.

When we come to the next section we find that the section begins by dealing with the case of a return as to which the Income-tax Officer is satisfied. In that case he assesses on the basis of the return. It then goes on to deal with a case where the Income-tax Officer has reason to believe that a return made is incorrect or incomplete, and the language of the statute imposes upon the Income-tax Officer the duty of serving upon the assessee a notice requiring him either to attend at the Income-tax Officer's office or to produce any evidence on which such person may rely in support of the return. The meaning of that clause is that when a return is made the Income-tax Officer shall not reject it and take some other basis as the basis of assessment without giving the assessee an opportunity to appear before him and give any evidence which he may desire to give. The power under clause (4) of section 22 is a power to the Income-tax Officer which has reference to accounts and documents and to no other form of evidence. The right under section 23 (2) is a right to call any evidence that the assessee may desire to call.

The last clause of section 23 deals with three different cases and for that reason perhaps the section is not so clearly drafted as it might be. It begins by taking the case of an assessee who makes no return at all and it says that the Income-tax Officer shall assess him to the best of his judgment. It then deals with the case of a person who has been ordered to produce accounts or documents and has failed to comply with the requirements. His is the same fate; the Income-tax Officer makes the assessment to the best of his judgment. It then deals with the third case—the case of a person who having made a return fails to comply with all the terms of a notice issued under subsection (2) of section 23. Upon that the contentions that are raised are, first, that no notice to produce accounts or documents can validly issue after the return is filed and, secondly, that if in fact a notice is issued under section 23 (2) it is impossible for the assessee to be penalized for the mere non-production of accounts; in other words, the second case contemplated by clause (4) of section 23 is no longer a case of which the assessee can be deemed to be an instance.

In my judgment, the exposition which the Commissioner of Income-tax has given is correct. He points out that the sub-section contemplates three distinct cases and, to my mind, it is abundantly shown by him that there is no warrant in the statute for saying that after a return is made the power given by clause (4) of section 22 is gone. The only ground which I have discovered for that opinion is the insertion of the harmless words "having made a return" into clause (4) of section 23. It seems paradoxical and improbable that the making of a return should put an end to the power of the Income-tax Officer to require the production of accounts. One would naturally suppose that the Income-tax Officer having seen a return may in some cases be in a better position than he would otherwise have been to say whether he thinks it necessary to inspect books of accounts or other documents or not.

But apart from that question it is at least extraordinary that a limit upon the power given by clause (4) of section 22 should be made in the dubious and inferential manner which is suggested, namely, by the words "having made a return" being inserted in clause (4) of section 23. In my judgment, there is no basis either as a matter of business or as a matter of construction for the opinion that the moment a return is filed the right of the Income-tax Officer to require the production of accounts under section 22 (4) is gone.

If that be so, the next question is whether it can be contended that because in fact a notice under clause (2) of section 23 was served upon this firm the power provided by clause (4) of that section to meet a case of withholding of accounts can no longer be exercised. In my judgment, there is no ground for that contention either. The Income-tax Officer in this case had asked the assessee first of all, to produce their books, secondly to attend upon him and thirdly, at the same time, to produce any other evidence they like. If the assessee is not in default, if they produce their books and attend, then, whether they produce other evidence or not, it will no doubt be for the Income-tax Officer to proceed against the assessee under sub-section (3) of that section. But if when the date comes it turns out that the assessee is withholding their books of account, but want to produce some other evidence, it seems to me reasonably plain that the Income-tax Officer may well say "You are in default for withholding your accounts. You will be dealt with on that basis. In the absence of available accounts neither argument nor other evidence is anything but a waste of time. It is *mera palpatic*. You will be treated as defaulters and in no other way". In my judgment that is what the statute intends. The statute intends that persons who deliberately make default in producing their accounts when asked to do so under clause (4) of section 22 shall be treated as defaulters and that the Income-tax Officer shall make the assessment to the best of his judgment.

It has been said that the Income-tax Officer must proceed in a judicial manner and section 37 has been mentioned in this connection. Fundamentally no doubt the Income-tax Officer must proceed in a judicial spirit and come to a judicial conclusion upon properly ascertained facts; though I would point out that the Income-tax Officer is not a court, he has not the procedure of a Court and he is to some extent a party or judge in his own case. However true it be and for whatever purpose it be true that the assessment to income-tax is to be done in a judicial manner, the first thing which must be laid down as a condition before a person can complain of any departure from this principle is this, that he too must produce the evidence which the law requires him to produce. It is idle and absurd for a person who has books of accounts and deliberately withholds them to complain of not being treated in a judicial manner. The judicial manner is a manner which proceeds upon evidence, and the basis of the statute is to see that available evidence is produced. It is then and only then that the assessment is to be made upon a judicial consideration of the evidence. Otherwise it is to be made "to the best of his judgment" and *brevi manu*.

In my judgment, there is no foundation for the assessee's contention on either of the points that have been referred to us. It seems to me, therefore, that the answer to these two questions should be, as I have indicated; to the first "No", to the second "Yes".

It only remains to mention certain cases which have been drawn to our attention. One is a decision of the High Court of Patna *Brijraj Ranglal v. Commissioner of Income-tax, Behar and Orissa*(1). In that case it would appear that the learned judges were not satisfied that a notice under section 22 (4) had been issued at all. They seem to think on the basis of the words "having made a return" under section 23 (4) that the power to call for books and documents is limited to the period prior to the filing of the return. But they say that "even if we assume that notice under section 22 (4) can be issued after a return has been filed, such notice not having been issued in this case summary assessment was illegal". It appears to me, therefore, that the view that the right to issue a notice under clause (4) of section 22 comes to an end on the making of a return was not essential to the decision in that case; but, in any event, I disagree with that opinion. It seems to me to have no merits whether as a matter of business or of construction of the statute.

The next case to which we were referred was the case of *Duni Chand Dhani Ram v. The Commissioner of Income-tax, Punjab* (2) decided by Mr. Justice LeRossignol and Mr. Justice Martineau. That was a case, where it seems to me that no law was laid down which is not in harmony with the view which I have endeavoured to express. That was a case where an assessee had made a return of his income. He was called upon to produce his books of account and he did produce his books of account. That being so, he was in the position of a man who must, under clause (2) of section 23 be given a proper opportunity to support his own return by such evidence as he desires and whether his return was supported by further evidence or not, the Commissioner was bound to assess him not, on the footing that he was a defaulter but on the footing that his return ought to be accepted save in so far as there might be good reasons for criticising it. The learned judges in that case, so far as I can see, have laid down no law to the effect that a person who is in default by wilful failure to produce accounts is not within the summary power given by clause (4) of section 23. Another case to which we have been referred is a decision of Mr. Justice Greaves and Mr. Justice Mukherji of this Court in the case of *Nirmal Kumar Singh Nowlaksha v. The Secretary of State for India in Council* (3). There, again, we have a case of an assessee who made a return and produced his accounts. At the time when he produced his accounts various matters were gone into between his Gomastha and the Income-tax Officer. Without giving a proper notice requiring him to produce such evidence as he might desire in support of his return the Income-tax Officer assessed him upon a basis inconsistent with his return and in these circumstances one learned Judge thought that the statute had been substantially complied with and the other learned Judge (Mr. Justice Mukherji) took the view that the informality was one which had not been waived and could not safely be ignored. In the course of that judgment there is not only nothing to the effect that the power to call for accounts must be exercised before the making of the return, but that judgment supports what the Income-tax Officer has done in this case.

Two cases have been drawn to our attention on the part of the Advocate General. One contains some expressions in a judgment of my own in

(1) 2 I.T.C. 458.

(2) 2 I.T.C. 188.

(3) 2 I.T.C. 20.

an Income-tax reference heard on the 18th of January, 1927, in the matter of *Ram Kissen Das Bagri v. Commissioner of Income-tax, Bengal* (1) and the other is a judgment of Mr. Justice Walsh and Mr. Justice Banerji of the Allahabad High Court in *Chandra Sen Jaini v. Commissioner of Income-tax United Provinces* (2). There, too, the dictum in the Patna case to which I have referred was dissented from and there, too, it was held that a combined notice under section 22 (4) and section 23 (2) was a proper notice.

In these circumstances it appears to me that the questions put to us must be answered against the assesseees and that the assesseees must pay the costs of this Reference.

GHOSE, J.:—I agree.

BUCKLAND, J.:—I agree.

[249] IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Sir Murray Coutts Trotter, Kt., Chief Justice, Mr. Justice Beasley and Mr. Justice Madhavan Nair.

[19th April, 1928].

A.L.A.R. Brothers, Devakotta

Assesseees*.

v.

The Commissioner of Income-tax, Madras

Referring Officer.

Income-tax Act (XI of 1922), Sec. 10 (2) (iii)—Assessee carrying banking business with borrowed money—Advances therefrom to separate piece-goods business—Piece-goods business, closed before account year and loss of sums invested therein—Claim for deduction in respect of interest paid on piece-goods business capital—If allowable—Use of capital in account year, if essential.

The assesseees primarily carrying on banking business on borrowed capital, also traded in piece-goods as a separate department under a different name, financing the latter business with money borrowed by the banking business and charging interest on such advances. The piece-goods business having sustained severe losses was closed down in 1923-1924. On an assessment to income-tax based on the income of the account year 1924-1925, the claim of the assesseees to deduct the interest paid on that part of their borrowed capital employed in the piece-goods business was disallowed on the ground that those sums having been lost in previous years were no longer available as capital of any business done by them in the account year.

Held, that the sums employed in the piece-goods business having been in their origin money borrowed as capital, interest paid thereon was allowable as a deduction under Sec. 10 (2) (iii) of the Income-tax Act, even though those sums did not continue to be available for the purposes of the business in the account year.

Case [Referred Case No. 19 of 1927] stated under section 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras for the opinion of the High Court in compliance with the order of the High Court, dated 2nd December, 1926.

* (1929) I.L.R. 52 Mad. 296; 55 M.L.J. 600; 28 L.W. 616; A.I.R. 1928 Mad. 1249.
(1) 2 I.T.C. 324. (2) 3 I.T.C. 17.

CASE.

In pursuance of the above order I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court.

2. The petitioners are A.L.A.R. Brothers, Devakotta, who are assessed to income-tax as an unregistered firm.

3. They have banking and other businesses at several places in this Presidency and in Burma. To each of these businesses they have allotted capital, and for each business separate sets of accounts are maintained so that the profit or loss of each business can be separately worked out.

4. They have a banking business at Madras known as the A.L.A.R. Firm. This business is almost wholly carried on with borrowed capital. In the year 1910 they opened a piece-goods business at Madras under the name of Ramaswami & Co., and financed it from time to time with the money borrowed by their banking business. According to Chetti custom interest was being charged in the accounts of Ramaswami & Co., on advances made by the A.L.A.R. Firm, corresponding credit being given in the accounts of the latter.

5. The piece-goods business sustained severe losses and was finally closed in 1923-24. The total losses up to that year were ascertained to be over 10 lakhs. The loss of each year was allowed in the assessment made on the petitioners in the succeeding year.

6. In the year of account 1924-25 Ramaswami & Co., made no purchases or sales and maintained no separate accounts. There were outstandings to the extent of Rs. 79,000, but most of them were irrecoverable. No active steps were taken to realise any of them. Some of the debtors were insolvents. When the business was closed in 1923-24, it was found that advances made to it by the A.L.A.R. banking firm amounted to Rs. 11,09,425 practically the whole of which was lost. In spite of such loss the sum of Rs. 11 lakhs was shown in the books of the A.L.A.R. firm as an outstanding due to that firm, and a notional credit entry of Rs. 1,07,653 was made as representing the interest supposed to have been received from Ramaswami & Co., on such advances, though as a matter of fact Ramaswami & Co., had ceased to exist and there were no available assets of that business out of which the A.L.A.R. Firm could recover even partially the advances made by it.

7. In assessing the profits of the A.L.A.R. banking firm in the following year (1925-26) the Income-tax Officer treated this notional credit of interest *viz.*, Rs. 1,07,653 as a business receipt in accordance with the entries in the books, and similarly allowed as business expenditure the whole of the interest on borrowed capital debited in the books. The petitioners claimed that the above sum of Rs. 1,07,653 ought to be deducted from the computed profits of the A.L.A.R. banking business as the said sum represented according to them a loss sustained by Ramaswami & Co., in the piece-goods business in the year of account. The Income-tax Officer rejected the claim on the ground that the petitioners had not carried on any business in the name of Ramaswami & Co., in the year of account and could not therefore have sustained any such loss in that year. An extract of the Income-tax Officer's order is appended, Exhibit A.*

8. On appeal the Assistant Commissioner held that the sum of Rs. 1,07,653 had been wrongly taken into account as a receipt of the petitioner's banking business. But he held that if this receipt shown in the books was to be ignored, a proportion of the interest shown as paid on capital borrowed by the banking business should also be left out of consideration on the ground that part of the capital borrowed had not been used in any business in the year of account as it had been lost in the piece-goods business in the previous years and was therefore no longer available. He accordingly computed the profits of the banking business by leaving out of account the receipt of Rs. 1,07,653 and disallowing under the head of interest payments a sum bearing the same proportion to the total of such payments as the capital used and lost in the piece-goods business bore to the total borrowed capital of the banking business. The interest so disallowed amounted to Rs. 99,571. An extract of the Assistant Commissioner's order is appended—Exhibit B.*

9. The petitioners applied to the Commissioner for a revision of the Assistant Commissioner's order and also for a reference to the High Court under section 66 (2) of the Income-tax Act. My predecessor refused their requests. Copies of his orders are appended—Exhibits C* and D.*

10. On an application under section 66 (3) of the Act the High Court passed the following order:

"That the applicants herein do file in Court the points on which they want the Commissioner of Income-tax to state a case to the High Court in a clear and concise form and serve a copy of the same on the Commissioner of Income-tax, Madras, and that after such service the said Commissioner of Income-tax, Madras, shall state a case to the High Court, Madras on the facts which in his opinion bear upon the question, and

(2) that this application be posted for hearing after the receipt of the statement from the Commissioner of Income-tax, Madras."

11. After a discussion with me the Vakil for the applicants has now formulated the following question (and I believe has filed it in Court):

"If a person who is carrying on a banking business borrows money and invests it in a separate piece-goods business and that business subsequently fails and the sum invested is lost, can interest on the borrowed money be lawfully *claimed* as a deduction under section 10 (2) (iii) in computing the profits and gains of the banking business for the year of account following the year of the loss?"

12. Section 10 (2) (iii) of the Act runs as follows: "in respect of capital borrowed for the purposes of the business, where the payment of interest thereon is not in any way dependent on the earning of profits, the amount of the interest paid". As I understand this clause, it provides for an allowance out of the profits and gains of a business in the year of account, of the amount of interest paid in respect of capital borrowed and utilised or employed in the business. The expression "borrowed for the purposes of the business" must, it seems to me, be taken to mean borrowed with a view to its being employed in the business and actually so employed in the year of account for the purposes of earning or producing the profits and gains of that year. In other words, what determines that a particular sum is borrowed

for the purposes of the business is not the intention of the borrower at the time of the borrowing whether carried into effect or not, but the actual utilisation of the sum for producing the profits and gains of the business in the year of account.

13. The contention of the petitioners is that the whole of their borrowed capital was borrowed for the purposes of their banking business and that it was one of those purposes to finance Ramaswami & Co. My answer to that must be that the profits and gains against which this allowance is claimed are those of the year of account 1924-25 and that in that year, it could not have been one of the purposes of the petitioner's business to supply funds to Ramaswami & Co., since the business done under that name had ceased to exist. The sums advanced to Ramaswami & Co., had been lost and were no longer available to be employed as capital of any business that was being done by the petitioners. In my opinion, therefore, the question must be answered in the negative on the ground that the sum on which interest is claimed was not capital employed in the petitioners' business in the year of account.

K. V. Krishnaswami Iyer and V. Rajagopala Aiyar, for the assesseees.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

The assesseees here are a Nattukottai Chetti firm who trade under the Vilasam of A.L.A.R. and their primary business is the usual Nattukottai Chetti business of banking and money-lending. They also trade in other ways and under the style of Ramaswami & Co., did a considerable piece-goods business in Madras which was opened in 1910. A.L.A.R. traded almost entirely on borrowed capital. The question is whether they are entitled to deduct from their income-tax assessment interest paid on that part of the borrowed capital which they had put into Ramaswami & Co. That branch of their business was unsuccessful. It had to be closed in 1924 and it was found to have sustained a loss of Rs. 11,00,000 odd. Substantially two points were put forward against the claim of the assesseees to make the present deduction. It was said first that the business of Ramaswami & Co. was quite separate and distinct from that of A.L.A.R. and that interest paid on money devoted to the purpose of providing trading capital for Ramaswami & Co. was not a deduction that could be allowed in the assessment of A.L.A.R. For this on the findings we can see no warrant. There is nothing in a name; Ramaswami & Co., in effect was A.L.A.R. and the case does not seem to us to be different from that of two departments of one big store. Spencer & Co., Limited, to take a familiar instance, carry on the business of Chemists and Druggists at one end of their buildings and that of haberdashers at the other end, and for all we know, they may for their own purpose keep the accounts of these two branches of their activities separate. It is obviously important for a modern multiple store like Whiteleys, or Herrods, or Spencers here to know how each branch of their business is doing, whether it is making a profit or a loss, so that, if one particular activity is shown to be carried on at a loss it would be open to them to close down that branch of their general business. Nor does it seem to matter that the piece-goods business conducted under the name of Ramaswami & Co., was carried on in a separate building in another part of Madras. In our opinion the findings preclude any inference that these were two separate and distinct businesses.

The second point taken was that, as the piece-goods business had been shut down in the year 1924 and did not function in the year of assessment, 1924-25, it cannot be said that the capital which had been borrowed was employed in the business during the year of assessment. The money was borrowed for the purposes of the business and was employed in the business for its purposes until it was lost. Nevertheless interest had to be paid on it and the test seems to us to be not whether it continued to be available for the purposes of the business during the year of assessment, but whether it was in its origin money borrowed as capital for the assessee's business and whether interest was in fact paid on that borrowed capital (existing or lost) during the year of assessment. We therefore, answer the question propounded in the affirmative, safeguarding ourselves by saying that the word 'separate' in the question framed is perhaps an unfortunate ambiguity and on the facts of this case means no more than that the business was carried on by A.L.A.R. in separate departments of which the unfortunate piece-goods department conducted under the style of Ramaswami & Co. was one. Costs fixed at Rs. 250 will be paid to the assessee by the Commissioner of Income-tax.

[250] IN THE HIGH COURT OF JUDICATURE AT RANGOON.

Before Mr. Justice Cunniffe and Mr. Justice Baguley.

[30th April, 1928.]

A.K.A.C.T.V. Chettiyar Firm

*Assessee.**

v.

The Commissioner of Income-tax, Burma.

Referring Officer.

Income-tax Act (XI of 1922), Sec. 66 (2) and (3)—Application to Commissioner to state a case on points of law refused—Assessee applying to High Court for a case on different points of law—Maintainability.

On an application to the High Court under section 66 (3) of the Income-tax Act, the Commissioner of Income-tax cannot be required to state a case on points of law different from those on which he was asked to state a case on an application under section 66 (2).

Application [Civil Miscellaneous Application No. 22 of 1928] under section 66 (3) of the Income-tax Act (XI of 1922) for an order directing the Commissioner of Income-tax, Burma to state a case for the opinion of the High Court.

Venkatram, for the Assessee.

A. Eggar, Government Advocate, for the Crown.

JUDGMENT.

This is an application on the part of the A.K.A.C.T.V. Chettiyar firm of Wakema. It is made under section 66, sub-section (3) of the Indian Income-tax Act. The application seeks for a mandamus against the Commissioner of Income-tax requiring him to state a case on two points of law. The points of law are alleged to arise out of an assessment of the firm to income-tax, but

whatever merits they may have, it is our opinion that we cannot consider them, for this very simple reason, that when the Commissioner was approached on the 13th of August, 1927, he was asked to state a case based upon four (as far as we can see) quite different points of law. Two of these points have been jettisoned and for the two remaining points, the points before us have been substituted. It appears to us that the intention of the language of sub-section (3) of section 66 is perfectly clear. Sub-section (3) runs as follows:—

"If, on any application being made under sub-section (2), the Commissioner refuses to state the case on the ground that no question of law arises, the assessee may, within six months from the date on which he is served with notice of the refusal, apply to the High Court and the High Court, if it is not satisfied of the correctness of the Commissioner's decision, may require the Commissioner to state the case and to refer it, and on receipt of such requisition, the Commissioner shall state and refer the case accordingly."

It appears to us quite obvious that what is meant by the language of the section is that the Commissioner shall be required to state a case upon the points of law, or at any rate, one of the points of law which he was considering. If the assessee were permitted to shift his ground from a legal point of view without any check upon him, it appears to us that the whole of the consideration by the Commissioner before any application reaches this Court would be rendered abortive.

In these circumstances and on this preliminary point, this application must be dismissed, with costs five gold mohurs in favour of the Crown.

[251] IN THE HIGH COURT OF JUDICATURE AT CALCUTTA.

Before Sir George Rankin, Kt., Chief Justice, Mr. Justice Buckland and Mr. Justice Mukerji.

[16th May, 1928.]

Messrs. Turner Morrison & Co., Ltd.

.. Assessee.*

v.

The Commissioner of Income-tax, Bengal

.. Referring Officer.

Income-tax Act (XI of 1922), Secs. 4 (3) (vii) and 12—Assessee carrying on business as Managing Agents of companies—Winding up of one company—Sums paid to assessee as compensation for loss of office therein—If income arising from business—Assessability.

Where the assessee carrying on business inter alia as Managing Agents and Agents of a number of companies and firms were paid a sum of Rs. 2½ lakhs as compensation for loss of their office as Managing Agents of a company voluntarily wound up,

Held, that the sum so paid was income assessable under Sec. 12 of the Income-tax Act and being a receipt arising from business was not exempt from assessment under Sec. 4 (3) (vii) of the Act.

Case stated under section 66 (2) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, Bengal, for the opinion of the High Court.

CASE.

In accordance with the provisions of section 66 (2) of the Indian Income-tax Act, 1922 (XI of 1922) and at the request of Messrs. Turner Morrison & Co., Ltd., the Assessee, I have the honour to refer to the Hon'ble High Court a question of law as hereinafter stated arising out of the assessment made on the Assessee for income-tax for the year 1926-27, the assessment being made *inter alia* on a sum of Rs. 2,25,000 received by them from the Cossipur Sugar Works Ltd., in liquidation under the circumstances stated below.

2. The Assessee carries on business in Calcutta as merchants and also as Managing Agents and Agents of a great many companies and firms. They have branches in Bombay and Chittagong.

3. The Cossipur Sugar Works, Ltd. (hereinafter called the Company) was incorporated as a company in the year 1909 and under Article 87 of the Articles of Association, the Assessee (then an unincorporated firm of the name of Messrs. Turner Morrison & Co.) as from time to time constituted, were appointed the Managing Agents of the Company, but there was nothing in the said articles regarding their appointment for any fixed term of years.

4. The Assessee was the registered holder of 6,683 shares out of a total of 10,000 shares of Rs. 100 each. Thus 66.83 per cent. of the share capital was held by the Assessee.

5. The Company had no Directors, but was managed by the Assessee as Managing Agents. The registered office of the Company was 4, Council House Street, the office of the Assessee.

6. Under Art. 87 of the Articles of Association of the Company the remuneration of the Managing Agents was to be fixed by the Company in General Meeting. This remuneration was varied from time to time. The last Resolution of the Company was passed on the 14th March, 1924, fixing the remuneration for the year ending 31st October, 1924, at Rs. 1,500 a month with commission. The total remuneration (including commission) received by the Managing Agents in 1923 and in 1924 was Rs. 48,332 and 48,424 respectively.

7. There was no contract actually executed between the Company and the Assessee for their services as Managing Agents of the Company. It was at the option of the Company to vary the remuneration from time to time and the Assessee was at liberty to terminate their own appointment as Managing Agents at their option.

8. On the 16th January, 1925, at an Extraordinary General Meeting of the Shareholders of the Company the following Resolution which was passed as an Extraordinary Resolution at the Extraordinary General Meeting of the Shareholders on the 2nd January, 1925, was confirmed as Special Resolution:—

“That the Company be wound up voluntarily and that Messrs. Harold Collman Edmondson, and Townley Walter Harding both of No. 4, Council House Street, Calcutta, Merchants, Directors of Turner Morrison & Co., Ltd. be, and they are hereby, appointed Liquidators for the purpose of such winding up, with joint and several powers.”

9. At the above meeting, the following Resolution was also passed:—

“That an amount of 2½ lakhs be paid to Turner Morrison & Co., Ltd., as compensation for their loss of office as Managing Agents of the Company.”

10. The Assessee claimed this sum of Rs. 2½ lakhs as a receipt of casual non-recurring nature not arising from business or the exercise of a profession, vocation, or occupation and so exempt under section 4 (3) (vii) of the Income-tax Act (XI of 1922). The Income-tax Officer considered this sum as a receipt from business and included this sum in their income for purposes of assessment. The Assessee appealed to the Assistant Commissioner who upheld the assessment. The Assessee thereupon applied under section 66 (2) of the Income-tax Act 1922 for a reference to the Hon'ble High Court.

11. The question of law which is referred to the High Court is as follows:—

On the above facts, is the said sum of Rs. 2,25,000 received by the Assessee exempt from taxation under section 4 (3) (vii) of the Indian Income-tax Act (XI of 1922)?

12. The Assessee urge in support of their contention, arguments which may be summarised as follows:—

(a) There being no agreement in the Articles of Association of the Company for the appointment of the Assessee as Managing Agents for a fixed term of years, they were liable to have the appointment terminated at any time by alteration of the articles.

(b) Their remuneration was, under the Articles of Association, to be fixed by Company in General Meeting. Thus it was at the option of the Company to vary the remuneration from time to time, with the reciprocal option to the Assessee to terminate their appointment at will.

(c) The Assessee could have no claim for damages or compensation for loss of their appointment as Managing Agents in the absence of a contract for any fixed period.

(d) The amount of Rs. 2,25,000 paid to them was by way of gift or testimonial, without any reference to their past relationship or their past services to the Company.

(e) The Assessee ceased to be the Managing Agents of the Company on the Resolution for the winding up of the Company being passed.

(f) The amount paid to the Assessee could not be said "to arise from business." The relationship as Managing Agents having ceased, there was no existence at the time no venture or concern in the nature of trade or business in connection with which the Assessee received the payment.

(g) To sum up, the relationship as Managing Agents having terminated, no business existed, and the sum paid was a voluntary gift and was of a casual or non-recurring nature not arising out of any business.

13. I am required under the Act to state my opinion in the matter which is as follows:—

(a) Though the winding up Resolution was passed on the 16th January, 1925, the Assessee had a claim to remuneration for the year commencing on the 1st November 1924 and there can be no doubt that this was borne in mind when the Resolution voting them Rs. 2,25,000 was passed. I am of opinion that this sum represents the remuneration for the year 1924-25 to which the Assessee were entitled legally and which if the Company had not been wound up, would beyond doubt have been assessed as income.

(b) The Assesseees had a controlling interest in the Company and in virtue of such interest got passed the Resolution regarding the payment of 2¼ lakhs to them.

(c) The payment would never have been made to them had they not been the Managing Agents of the Company, and therefore it accrued to them in virtue of their office.

(d) The Assesseees carry on business as merchants, and agents of a large number of firms and companies; and this sum received by them was not of a casual or non-recurring nature, but one usually received in course of business by firms carrying on the widespread business of the Assesseees.

I am, therefore, of opinion that the receipt of the money in question is a receipt arising from business as defined in section (2) (4) of the Income-tax Act and is not exempt from assessment under section 4 (3) (vii) of the Act as contended by the Assesseees.

Langford James and W. A. K. Page, for the Assesseees.

Sir B. L. Mitter, (Advocate-General) and S. M. Bose for the Crown.

JUDGMENT.

RANKIN, C. J.:—In this case, the Commissioner of Income-tax, Bengal, has stated to this Court for its opinion the question whether a certain sum Rs. 2¼ lakhs, received by the Assesseees is exempt from taxation under section 4, sub-section 3, clause (vii) of the Indian Income-tax Act, 1922. The sum in question is a sum which was voted to the Assesseees by the share-holders of a company called the Cossipur Sugar Works, Ltd. It appears that that company was passing a resolution for voluntary winding up. A firm which had previously carried on the business now carried on by the Assesseees had been nominated by the Articles of Association of this Company as their Managing Agents. No time was fixed throughout which they were to be the Managing Agents and no remuneration was settled for the office; but, in point of fact, the Firm and afterwards the Company, namely, the present Assesseees acted as the Managing Agents and during certain years which are mentioned in the letter of Reference, received about half a lakh of rupees annually for their trouble. Now, the business was coming to an end. The Cossipur Sugar Works, Ltd., was being wound up and the Resolution passed by the share-holders was that an amount of 2¼ lakhs of Rupees was to be paid to Messrs. Turner Morrison and Company Ltd., as compensation for their loss of office as Managing Agents of the Company.

The question which we have to decide is whether or not that sum which was paid to the Assesseees is a receipt not being a receipt arising from business or the exercise of a profession, vocation or occupation, which is of a casual and non-recurring nature and is not by way of addition to the remuneration of an employee. The Commissioner of Income-tax is of opinion that it cannot be predicated that it was not a receipt arising from business. I am of the same opinion.

We are dealing here with two companies. It is quite true that the Assessee Company was a shareholder of the Cossipur Sugar Works, Ltd. One Company was not only making a large payment to the other Company but stated that the reason of it was "as compensation for their loss of office as Managing Agents". We are not, therefore, considering a personal gift to a friend, and cases of that class may be put on one side.

It has been contended before us that, in view of the fact that the Managing Agency of the Cossipur Sugar Works, Ltd., came to an end by reason of the resolution to wind up, the payment of compensation for the loss of office cannot be a payment or receipt arising from business. Now, that contention has been urged upon us mainly on the basis of certain English cases which are addressed to a very different state of the law. The problem before the English Courts in the cases which have been cited before us was whether or not the payment in question was a perquisite of an office or employment. The scheme of the Indian Act is different. Section 4 sets out, in the first place, certain forms of income which are not to be exposed to income-tax at all; and it is in that connection that clause (vii) of sub-section (3) is enacted. When we come to the subsequent sections, we find that these sections beginning with section 6 deal with incomes under certain heads specified by the statute. Section 6 lays down these heads and the following sections deal with each of those six heads. When we come to section 10, we find that tax is payable under the head of "Business" in respect of the profits or gains of any business carried on by the Assessee; and section 12 which deals with the residuary heading "other sources" is expressed in this way: the tax shall be payable in respect of "income, profits and gains of every kind and from every source to which this Act applies (if not included under any of the preceding heads)". If therefore, a payment comes under clause (vii) of sub-section (3) of section 4, it is not covered by section 12 at all. In my judgment, we have to take the words of clause (vii) by themselves. We are not concerned for this purpose with the wording of section 10. We are vitally concerned with the wording of clause (vii) of the third sub-section of section 4. Whether or not an amount is profit or gain of any business is one question; whether it is "a receipt arising from business" is another question. We are concerned with the latter.

Now, the English cases go not upon any similar test. They go upon the question whether a certain receipt is a perquisite of an office. If it is not a perquisite of an office or a profit of business or trade, then it is not taxable. Consequently the class of cases, known as the Easter offering cases, *e.g.*, *Herbert v. McQuade*(1) and *Turner v. Cuxson*(2) are not, in the least, in point. In one case it was held that the person got the money, because he was the parson; therefore, it was a perquisite of the office. In the other case it was held that, although the curate would not have got the money unless he had been the curate of the parish, still he got it as a testimonial for his work and not, because he was curate. In the same way, in the case of *Cowan v. Seymour* (3) the question was whether or not the voluntary payment accrued to the person by reason of his office. That was the case of a person who had acted as the Secretary of a company. He was given what was called a testimonial. In view of the fact that it was a testimonial it was held that it was not a perquisite of the office which had come to an end. Similar considerations were canvassed in the cricketer's case, *Seymour v. Reed*(4) and in the Jockey's case, *Wing v. O'Connel*(5).

Now, in the case before us, we are not considering whether Messrs. Turner Morrison and Company Ltd., received this sum of money as a perquisite of an office. We are enquiring whether they received this sum of money as a receipt arising from business. They are a company that have several—it may be many—managing agencies. This is found as a fact by the Commissioner of Income-tax. They were given this sum of money because,

(1) 4 Tax. Cas. 489 ; (1902) 2 K. B. 631.

(2) 2 Tax Cas. 422 ; 22 Q. B. D. 150.

(3) 7 Tax Cas. 372 ; (1920) 1 K. B. 500.

(4) 11 Tax. Cas. 625 ; (1927) A. C. 554.

(5) (1927) Ir. R. 84.

without notice to them, in the middle of the year, one of their managing agencies was being brought to a close. In the circumstances, it was thought right to given them this amount by way of compensation for their sudden dismissal. In my judgment, it is impossible to say that the receipt is not a receipt arising from business and that is the statutory test which in this country has to be applied. It was not contended before the Commissioner that this case, if it did not come under section 10, would not, apart from this exemption clause, be hit by section 12. We are not concerned, therefore, to find yea or nay, whether Mr. Justice Rowlatt's view is right or not in the case of *Seymour v. Reed*, (1) i.e., whether the payment for the loss of the Managing Agency would be a profit of the business. If it does not come under section 10, then it comes under section 12. And the observation in the cricketer's case that such wind-fall as was there before the House was not income does not avail in this case. There is no doubt upon the Indian Act that the payment in the present case is income within the meaning of section 12 unless it is saved by section 4 (3) (vii).

In these circumstances, it seems to me that the Commissioner of Income-tax was right in deciding that the exemption relied on was of no use to the Assesseees and that income-tax was rightly assessed.

Costs must be paid by the Assesseees.

BUCKLAND, J.:—I agree.

MUKERJI, J.:—I agree.

(252) IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Mr. Justice Mukerji and Mr. Justice Bennett.

[17th May, 1928.]

The Indian Turpentine and Rosin Co., Ltd.

.. Assessee.*

v.

The Commissioner of Income-tax, United Provinces

.. Referring Officer.

Income-tax Act (XI of 1922), Sec. 10 (2) (ix)—Company purchasing resin factory from Government—Government supplying crude resin at cost price plus royalty—Additional royalty to be paid on company's excess profits over 15 per cent.—Claim for deduction of additional royalty.

Under an agreement entered into between the assessee Co. and the United Provinces Government for the sale of resin factory by the latter, the Government in addition to taking up half the shares in the Co., was to supply through its Forest Department crude resin at the cost of labour and delivery plus a royalty of Re. 1 per maund and if the profits of the Co., in any year exceeded 15 per cent., a further payment of 40 per cent of the excess profits was to be made in the following year as additional royalty. On an assessment to income-tax on the profits of the accounting year 1926-27, the Co. claimed to deduct as business expenses the share of its profits in 1925-26 paid in the accounting year as additional royalty to Government.

HELD, that the sum paid as additional royalty was price paid for the supply of resin and hence was expenditure incurred solely for the purpose of

* (1928) 26. A. L. J. 1829. : A.I.R. (1929) All. 118.

(1) II Tax Cas. 625 ; (1927) A.C. 554.

earning profits deductible under Sec. 10 (2) (ix) of the Income-tax Act.

Case (Mis. Case No. 245 of 1928), stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, United Provinces for the opinion of the High Court.

CASE.

The business of the Indian Turpentine and Resin Company, Limited, belonged originally to the Government of the United Provinces and was known as the Government Turpentine and Resin Factory at Ciutterbuckgunj in the Bareilly district. The Local Government sold the concern to a syndicate in accordance with the agreement, dated September 1, 1923, of which a copy, with a copy of the second schedule, is attached in Appendix I. A company was floated by the Syndicate in 1924 with a capital of twelve lakhs of rupees of which shares to the value of six lakhs of rupees were allotted to the Local Government.

2. Among other terms in the agreement the Local Government undertook to sell not more than 100,000 maunds of crude resin every year to the Company (clause 13). It was further agreed as laid down in clauses 7 and 8 of the agreement in the second schedule that, besides the cost of collection and transport, the Company would pay only an allowance of one rupee per maund net weight of crude resin delivered to the Company as royalty to the Forest Department, and in addition to a share of net profits of the Company to be calculated in accordance with clause 30 an additional royalty on crude resin supplied. Clause 30 runs:— This share shall be calculated as follows:—

“If the profits of the Company in any year exceed 15 per centum of the capital of the Company ranking for dividend then the Company will pay the Forest Department as additional royalty such proportion of 40 per centum of the amount by which the profits exceed the above-mentioned 15 per centum as the number of maunds of crude resin either supplied by the Forest Department to the Company or collected and extracted by the Company from the channels made available by the Forest Department in the preceding tapping season (or if the year coincides with the tapping season then in the tapping season concerned) bears to the total number of maunds of crude resin received by the Company in that period.

The profits of the Company for the purposes of this agreement shall be such profits as may be ascertained by the Company's Auditors from year to year after deducting all working and other expense chargeable against revenue and proper depreciation on all buildings, machinery, plant and materials. The certificate of the auditors of the Company regarding the amount due to Government under this clause shall be accepted.”

3. The Company was assessed to income-tax on September 27, 1927, on the basis of its profits in the financial year (its accounting period) 1926-27. In framing his assessment the Income-tax Officer, Babu Sital Prasad (*vide* extract copy of order in Appendix II) refused to allow as a business expense in the year in question, the sum of Rs. 24,328-12-0 paid out of the profits of the year 1925-26 as additional royalty to the Local Government in accordance with the Director's proposals on the accounts for that year (extract copy of report which was issued on August 7, 1926, enclosed—Appendix III), although Thakur Ram Singh the Income-tax Officer, who assessed the Company in 1926-27, had said that this

sum would be admissible in the next year (extract copy of order attached—Appendix IV).

4. The Company appealed against this decision to the Assistant Commissioner of Income-tax, who upheld the order of the Income-tax Officer. A copy of the relevant part of the appellate order is also attached (Appendix V).

5. The Company has now asked that a case be stated for the decision of the High Court on the point whether the action of the Income-tax Officer in disallowing the sum of Rs. 24,328-12-0 was correct. A copy of its petition is enclosed in Appendix VI.

6. The point of law which arises is:—

Is the share of the profits of the Company in 1925-26, which was paid to the Government of the United Provinces as additional royalty in 1926-27, expenditure incurred solely for the purpose of earning the profits of the Company assessable in 1926-27 within the meaning of section 10 (2) (ix) of the Indian Income-tax Act?

7. The Commissioner is of opinion that the answer to the question is in the negative. He would add that he disagrees with the view of the Income-tax Officer who made the assessment in 1926-27, and has taken steps to raise the assessment if the High Court answers the above question in the negative.

Kailasanath Katju, for the Assesseees.

Uma Shankar Bajpai, for the Crown.

JUDGMENT

BENNETT, J.:—This is a reference by the Commissioner of Income-tax in the following terms in regard to the business of the Indian Turpentine and Resin Company, Limited: "Is the share of the Company in 1925-26, which was paid to the Government of the United Provinces as additional royalty in 1926-27 expense incurred solely for the purpose of earning the profits of the company assessable in 1926-27 within the meaning of section 10 (2) (ix) of the Indian Income-tax Act"?

The origin of the Company is as follows:—Originally the Government of the United Provinces owned a factory for the production of resin in Bareilly and that factory received crude resin from the Forest Department. In the year 1923 the Local Government desired to have the factory transferred to a company and accordingly it entered into a deed of sale and an annexed schedule of agreement with a certain Syndicate of three gentlemen who eventually floated the Company called the Indian Turpentine and Resin Company Limited. The primary object of the Local Government was to have an assured market for the crude resin obtained from its Forest Department. Accordingly, in addition to becoming a shareholder to the extent of half the shares in a company to be floated, certain clauses were made in the second schedule of the agreement by virtue of which agreements were to be made each year between the Forest Department and the Company as to the amount of crude resin which was to be supplied in the following season by the Forest Department. This schedule

further provided in clause (7) that the cost of supply of the crude resin was to embrace:

- (a) The estimated expenditure of materials, labour and special staff.
- (b) A certain allowance for delivery.
- (c) An allowance of Re. 1 per maund net weight of crude resin as royalty.

Clause (8) provided:—

“In addition a share of the net profits of the company as described in clause 30 shall be payable to the Forest Department by the Company as additional royalty on the crude resin supplied.”

Clause 30 provides as follows: “In addition to the payments to be made by the Company to the Forest Department under clauses 16 and 27, a share of the profits of the company, as mentioned in clauses 8 and 26, shall be paid annually by the Company within three months of the close of each tapping season.

This share shall be calculated as follows:—

If the profits of the Company in any year exceed 15 per centum of the capital of the company ranking for dividend then the Company will pay the Forest Department as additional royalty such proportion of 40 per centum of the amount by which the profits exceed the above-mentioned 15 per centum as the number of maunds of crude resin either supplied by the Forest Department to the Company or collected and extracted by the Company from the channels made available by the Forest Department in the preceding tapping season (or if the year coincides with the tapping season, then in the tapping season concerned) bears to the total number of maunds of crude resin received by the Company in that period.

The profits of the Company for the purpose of this agreement shall be such profits as may be ascertained by the Company's auditors from year to year after deducting all working and other expenses chargeable against revenue and proper depreciation on all buildings, machinery, plant and materials.

The certificate of the auditors of the Company regarding the amount due to Government under this clause shall be accepted.”

The arrangement, therefore, is that a certain quantity of crude resin is supplied in a certain year and for that a certain price for cost of labour and delivery and Re. 1 royalty is paid during that year. In the following year a further payment is made which varies with the profits of the Company if those profits exceed 15 per cent.

The question before us is whether that extra sum paid in the following year is a distribution of profits by the company in which case it is liable to pay income-tax, or whether it is to be regarded as a business expense of the Company. It was held by the Income-tax Officer that as this royalty was dependent on the earnings of profits, therefore it was an allocation of profits to one of the biggest shareholders of the Company. That position, however, was abandoned in the Court of appeal before the Assistant Commissioner of Income-tax, because it was pointed out that if the Government sold all its shares in the Company, the Company would still have to pay the same amount of royalty. Therefore the payment could in no sense be regarded as an allocation of profits to one of the

co-sharers in the Company. It is merely an unconnected fact that Government are at present shareholders in the Company.

The grounds on which the Assistant Commissioner of Income-tax proceeded were that the additional royalty was calculated in a certain manner and the liability to pay it arose in a certain manner, both of which were connected with the profits earned by the Company. He held therefore that it could not be considered as a payment for resin supplied, nor could it be considered as an expense necessary for the earning of the profits of the Company. The case has been very ably argued before us and we consider that the relevant points are as follows:—

(1) We consider that the matter is analogous to the payment of a share of profits of a business to a managing director. The managing director gives his services to the business and after the close of any financial year he is given in the following year a proportion of the profits of the business. That proportion of the profits is counted as one of the expenses of the business incurred solely for the purpose of earning the profits of the business and therefore is not liable to assessment to income-tax under section 10 (2) (ix) of the Indian Income-tax Act.

(2) In considering the question as to whether this payment is profit of the Company or a business expenditure, we consider that the fact that in its annual balance sheets this would not be shown as profit available for distribution to the shareholders is a relevant fact. The profit is not available for distribution to the shareholders. It is to be paid for the cost of the crude resin supplied in the previous year.

(3) If the Company was calculating the cost of production of its resin, it would certainly have to take into account this additional royalty paid to the Government.

(4) As regards the definition of price, section 77 of the Indian Contract Act states "the sale is the exchange of property for a price." There is nothing in this definition which precludes the inclusion of this additional royalty as part of the price of the crude resin supplied to the Company. In the second schedule it is laid down that this payment is to be made to the Forest Department. This payment is made on behalf of the crude resin supplied and is part of the price of that crude resin. It is in no sense part of the consideration for which Government sold the factory in Bareilly.

(5) Looking at the origin of the agreement of sale between Government and the Syndicate which resulted in the eventual formation of the Company, we notice that the primary object of Government was to obtain a market for its resin.

In the order of appeal of the Assistant Commissioner of Income-tax it is stated that the Chief Conservator of Forests stated that, owing to want of previous experience in the matter the additional royalty was imposed merely by way of securing fair price for the crude resin supplied. This indicates that at the time of entering into the agreement in the second schedule Government and the syndicate were not in a position to ascertain what would be a fair charge for a royalty on the crude resin supplied. Accordingly a nominal royalty of Re. 1 per maund was taken and the agreement in clause 30 was made in order that if that amount proved to be too low a price in view of the market conditions, an extra sum would be paid to Government in order to bring the royalty to a proper figure.

In view of all these considerations we answer the enquiry in the affirmative and we consider that the sum of Rs. 24,328-12-0 paid out of the profits of the

year 1925-26 as additional royalty to the Local Government is a sum which should not be included in the assessment of income-tax on the profits of the Indian Turpentine and Resin Company, Limited. The Company is allowed the costs of this reference.

MUKERJI, J.:—I agree with my learned brother in answering the reference in the affirmative and in agreeing that the costs should be paid as directed by him. The operative portion of his judgment, therefore, stands as the judgment of the Court.

The facts of the case are given in detail by my learned brother. I have only to add one thing and it is this. In my opinion the correct answer to the question put to us can be had by answering a simple question. The question is this. What is the consideration for the money paid to the Local Government (being a part of the profits earned) when the profits earned exceed 15 per cent? It is clear that the payment is not made to the Local Government as "shareholders". The payment is made on account of resin supplied. If this is not the case, then there is no consideration whatsoever for this payment. I have not the least doubt that the sum in question paid to the Local Government was paid as the price of resin supplied and that therefore the money so spent was a part of the expenditure incurred solely for the purpose of earning the profits of the Company.

(253) IN THE HIGH COURT OF JUDICATURE AT BOMBAY.

Before Sir Charles Fawcett, Kt., Acting Chief Justice and Mr. Justice Mirza.

[22nd June 1928.]

Madhavadas Jethabhai

.. Assessee.*

v.

The Commissioner of Income-tax, Bombay

.. Referring Officer.

Income-tax Act (XI of 1922), Sec. 66 (2) and (3)—Commissioner refusing to state a case as time barred under Sec. 66-(2)—Application to Court under Sec. 66 (3), if lies—Specific Relief Act (1 of 1877), remedy thereunder.

The provisions of Sec. 66 (3) of the Income-tax Act are not applicable to a case of refusal by the Commissioner of Income-tax to state a case on the ground that the application therefor was made beyond the period of one month prescribed by Sec. 66 (2) of the Act. The remedy open in such a case is an application under Sec. 45 of the Specific Relief Act.

Civil Application No. 1030 of 1927 under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922), for an order to direct the Commissioner of Income-tax, Bombay, to state a case.

G. N. Thakor, for the Assessee.

J. Kanga, for the Crown.

JUDGMENT.

FAWCETT Ag. C. J. A preliminary objection has been taken, in this case, by the Advocate-General that the application does not lie to the High Court on its

* (1928) 30 Bom. L.R. 1114 : A.I.R. (1928) Bom. 434 (1).

appellate side in the form in which the application has been brought under the provisions of section 66 of the Indian Income-tax Act. The Advocate-General has pointed out that sub-section (3) of section 66 is limited to a case of refusal by the Commissioner to state a case on a particular ground, viz., the ground that no question of law arises. If there is such a refusal, then sub-section (3) enables an application to be made by the assessee to the High Court and the High Court to interfere, if it is satisfied of certain things.

Mr. Thakor for the applicant contends that sub-section (3) should be read as covering a refusal on any other ground such as the one in which the Commissioner's refusal was based in this case, viz., that the application to him to refer to the High Court the question of law arising out of this order had been made beyond the time of one month prescribed by sub-section (2). It seems to us impossible to construe sub-section (3) in a way that would be directly contradictory to its express terms. The Legislature having chosen to limit sub-section (3) to a case of refusal on the ground of no question of law arising, it would obviously be beyond our province to construe that section as covering a refusal on some other ground, especially as another remedy is open to the applicant under section 45 of the Specific Relief Act, as is shown, for instance, by the Privy Council case of *Alcock, Ashdown & Co., v. Chief Revenue Authority, Bombay*.⁽¹⁾ Our opinion is also re-enforced by a similar opinion expressed by the Calcutta High Court in *Kumar Sarat Kumar Roy v. The Commissioner of Income-tax, Bengal*.⁽²⁾ We do not think that we can permit the present application to be converted into an application under section 45 of the Specific Relief Act, in view of the fact that Rule 536 of the Original Side Rules, 1922, as revised in 1926, requires the application to be entitled in a certain manner and to be made on motion in open court before a Judge on the original side or a specially constituted bench. But we direct that the affidavits that have been filed in this case may be used in support or in answer to any such application. The application is accordingly dismissed with costs. Costs to be as on the appellate side scale.

(254) IN THE HIGH COURT OF JUDICATURE AT PATNA.
FULL BENCH.

Before Sir Courtney Terrell, Kt., Chief Justice, Mr. Justice Das, Mr. Justice Adami, Mr. Justice Wort and Mr. Justice Allanson.

[12th June 1928.]

Ram Khelwan Ugamlal

v.

Assessee.*

The Commissioner of Income-tax, United Provinces .. Referring Officer.

Income-tax Act (XI of 1922), Secs. 22, 23, 63 and 64—Notice under Sec. 22 (4), when issuable—Submission of return, effect of—Notice not stating section of Act, legality of—Form and service of notice, requisites as to—Scope of Sec. 63—Assessment based on report of estimated income by another Income-tax Officer, validity of.

HELD BY THE FULL BENCH: *The notice contemplated by Sec.*

(1) 1 I. T. C. 221

(1928) I. L. R. 7 Pat. 852 : A. I. R. (1928) Pat. 529.

(2) 2 I. T. C. 279.

22 (4) of the Income-tax Act can be issued to a person served with notice under section 22 (2) of the Act at any time before the final assessment, whether a return has been submitted or not. A notice not stating the section or sections of the Income-tax Act under which it is served is not illegal.

The assessee, a firm carrying on business at S. & P. in Bihar and Orissa and also at C in the United Provinces, submitted a return of the profits of the branch at S. & P. and in compliance with a notice under Secs. 22 (4) and 23 (2) produced their account books. The Income-tax Officer after examining them passed an order entered in the Order-sheet directing the assessee to produce the accounts of the business at C. This Order-sheet was shown to a partner of the assessee's firm who signed his name in its margin as an acknowledgment of the receipt of the notice. On failure to produce the accounts called for, the Income-tax Officer made an assessment under section 23 (4), including in the assessment the sum of Rs. 10,000 reported by the Income-tax Officer in the United Provinces as the estimated profits of the business at C.

HELD by the Division Bench, (Dawson Miller, C. J. and Ross, J.), that the assessee was properly served under Sec. 22 (4), no special form of notice thereunder being prescribed under the Act and that the mode of service specified in Sec. 63 was permissive and not exhaustive.

HELD further that the assessment was not contrary to the provisions of Sec. 64 as there was no assessment of the firm at C by the Income-tax Officer who merely reported his estimate of profits.

Case (Misc. Judicial Reference No. 141 of 1926), stated under Sec. 66.(3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, United Provinces, in compliance with the order of the High Court.

CASE.

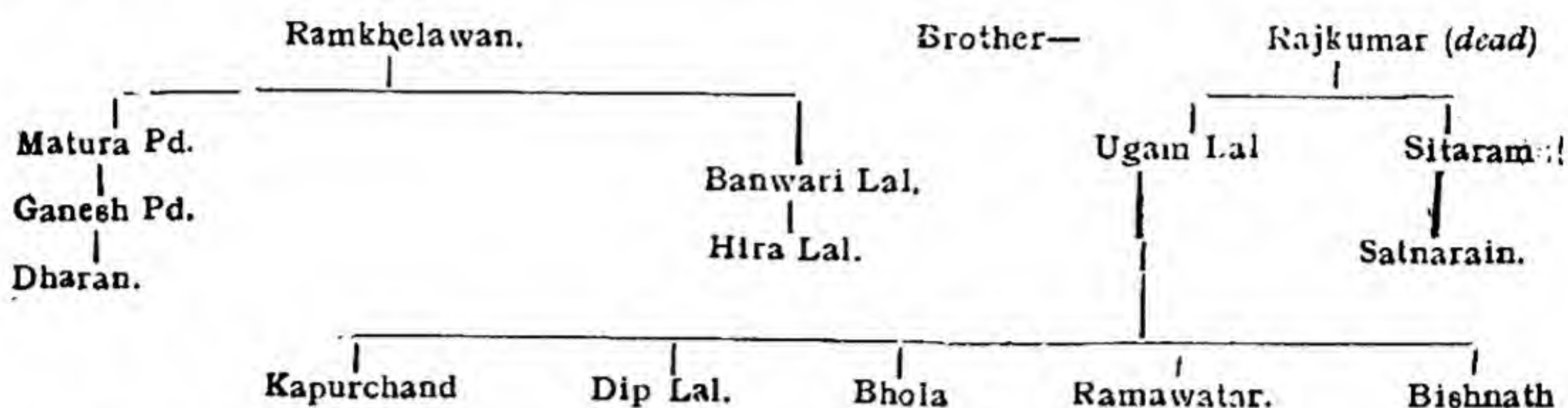
I have been directed by their Lordships to state a case for their decision on the following two points of law, arising out of the appellate order in the above assessment: Firstly, whether the production of the order-sheet to Banwari Lal by the Income-tax Officer was a proper service of a notice under section 22 (4), and secondly, whether, seeing that the income-tax in respect of the United Provinces firm of Ramawatar Hira Lal had already been assessed at 10,000, it was any longer open to the Income-tax Officer, Saran, to assess the income-tax of the Saran firm summarily under section 23 (4), because the books belonging to the Chilwaria firm had not, in fact, been produced.

2. The facts of the case are set out below: This reference has arisen out of the assessment order passed under section 23 (4) on 21-1-26, that is, in the year 1925-26 on the income of the "previous year" ending Kartik Badi, 1332 Fasli, corresponding to September or October 1924.

3. There is a firm at Siwan in the District of Saran carrying on business in the name of Ramkhelawan Sahu Ugam Lal, there is a firm at Pachrukhi in the District of Saran carrying on business in the name of Mathura Prasad Sitaram, while there is a firm styled Ramawatar Hira Lal carrying on business at Chilwaria in the Bahraich District in the United Provinces.

4. The genealogical table given below will show the relationship between the several persons after whom these 3 firms are styled, and it will be seen that, in the case of each firm, one name is taken from the branch of Ramkhelwan,

while the other name is taken from the branch of Rajkumar, the deceased brother of Ramkhelawan :



The Income-tax Officer, Saran, on receipt of information that the firm in the United Provinces was identical in constitution with the firm in Siwan and Pachrukhi, passed an order on the order sheet on 6-9-25 under section 22 (4) directing the assessee to produce the accounts of the Chilwaria business together with the original Bijaks and Bijak Bahis on 12-9-25, this order in the order sheet being signed by Banwari Lal, the son of Ramkhelawan. On 12-9-25, these accounts were not produced and an adjournment was given to the following date to enable the Income-tax Officer to examine certain other account books of the assessee. On this date, that is, 13-9-25, the assessee's Gumashta, Jamuna Prasad, promised to produce the accounts of the Chilwaria firm on a date after the Puja holidays, and 9-10-25 was accordingly fixed. On 9-10-25 Banwari Lal the son of Ramkhelawan appeared but without the account books, alleging that they were required by the Income-tax Officer, Bahraich, on 8-10-25, and on 21-1-26, the Income-tax Officer, Saran, on receiving a report from the Income-tax Officer, Bahraich, to the effect that the accounts had not been produced there on the ground that they were with the assessee in Saran District made an assessment under section 23 (4) in respect both of the income from the business in Saran and the income from the business in the United Provinces, the amount of profit, in the case of the United Provinces branch, being taken at the figure reported by the Income-tax Officer, Bahraich.

5. The contention of the assessee before me was that he was unable to produce the accounts of the Chilwaria firm because that was an independent firm in which they had only a part share, but before the Income-tax Officer, up till the time assessment under section 23 (4) was made, their contention was not that the Chilwaria firm was an independent firm, but that the accounts of that branch could not be produced because they were required in Bahraich by the Income-tax Officer there before whom, as a matter of fact, they were never produced and the contention that the constitution of the Chilwaria firm was different from the constitution of the Siwan firm was raised for the first time in the application under section 27 of the Act and dated 8-2-26 asking the Income-tax Officer to re-open the assessment.

6. Though the question whether the constitution of the firm in the United Provinces is identical with the constitution of the firm in Siwan is not a point at issue and I am not directed to discuss this point in the statement of the case, I shall endeavour, nevertheless for the satisfaction of their Lordships, to prove that the two firms are identical. As observed above, the contention that the firms were different in constitution was not raised before the application under section 27 was made on 8-2-26 and, on the other hand, Sitaram, Gumashta of the firm of Ramkhelawan Ugain Lal, made a statement on oath before the Income-tax Officer, Saran, on 5-9-25, a relevant extract from which I quote below :

“Ramkhelawan Ugam Lal have Arhat business at Chilwaria, District Bahraich, going by the name of Ramawatar Hira Lal.....The Malik (that is Ramkhelewan Ugam Lal) have a firm at Panchrukhi which goes by the name of Mathura Prasad Sitaram”

while, Banhari Lal, son of Ramkhelawan, made a statement on oath two days later extracts from which bearing on this point I note below:—

“The Pachrukhi firm goes by the name of Mathura Prasad Sitaram. This is a branch of the firm of Ramkhelawan Ugam Lal. We have a business at Chilwaria which goes by the name of Ramawatar Hira Lal. Before 1331-F, we had a business there in partnership with Jadu Sahu Mahadeo Lal of Siwan. It went there by the name of Jadu Sahu Ramkhelawan. The partnership was dissolved about 4 or 5 years ago”.

Copies of the full statement of Sitaram and Banwari Lal are attached to the statement of the case and are marked I* and II* respectively.

7. In the petition under section 27 the contention that these 3 firms were separate in constitution was raised for the first time. I note, however, that the Vekalatnama attached to this petition was accepted through this same Banwari Lal who had, in the previous September, stated specifically that the Pachrukhi firm is a branch of the firm of Ramkhelawan Ugam Lal, while they, that is, the firm of Ramkhelwan Ugam Lal with which he identifies himself, have a business at Chilwaria which goes by the name of Ramawatar Hira Lal. Again, it will be seen from the report of the Income-tax Officer, Bahraich, dated 22-10-25, copy of which marked III* is attached, that the Munib of the firm in Chilwaria stated before him that the account books could not be produced there because they were with the proprietor in village Nowranga, Pachrukhi P.O., District Saran, but village Nowranga is the home of Ramkhelawan and not the home of Balram who, it is now contended owns an 0-8-0 share in the business, the home of the latter being Kuluwan, another village in the Saran District.

8. Further, it is the custom when two families join in partnership to select the name of a representative of each family to form the designation of the firm. In the case of these 3 firms, however, only the names of members of Ramkhelawan and Rajkumar's family are found, but not the names of any member of the family of these other persons who are now claimed as partners, and this also supports my view that there are no partners in these firms outside the members of these two families.

9. Their Lordships have asked specifically for information on the points which I deal with below: Whether Banwari Lal, although his name was not one of those constituting the style of the firm, was in fact a member of the firm of Ramkhelawan Ugam Lal. The facts are as follows:—Banwari Lal is the son of Ramkhelawan with whom he is joint and the latter being an old man, the business is conducted by the son. In this connection, I would respectfully invite a reference to Banwari Lal's statement on oath on 7-9-25 in which he states “We have a business at Chilwaria which goes by the name of Ramawatar Hira Lal”. His use of the word “we” shows that he identifies himself with the business. This form of expression may be contrasted with the statement of Sitaram Gumashta made on 5-9-25 which is to the following effect “Ramkhelawan Ugam Lal have Arhat business at Chilwaria..... The Malik have a firm at Pachrukhi.” On the evidence, the only finding I can arrive at is that Banwari Lal is a member of the firm of Ramkhelawan Ugam Lal

and that indeed all the 3 firms referred to above, though trading under different names at different places, are identically constituted, namely, by all the male members of the branch of Ramkhelawan and of the branch of Rajkumar.

10. Banwari Lal conducted the case before the Income-tax Officer all along as a member of the firm and as their agent. He produced the accounts before the Income-tax Officer on different dates and filed petitions when necessary. The Vekalatnama in the section 27 application was accepted through him and the appeal petition was accepted through him, while he also signed an application made before me on 6-7-26 asking for an adjournment in the hearing of the review case and the application for reference.

11. Information is also asked for on the point whether the two families, one of which is represented by Ramkhelawan and the other by Ugam Lal and his brother Sitaram, are joint. From the evidence, the only finding I can come to is that they are joint in business though separate in mess. This conclusion is based on the statement on oath made by Banwari Lal on 7-9-25 to the following effect: "Ugam Lal who is my first cousin being the son of my uncle Rajkumar died 2 years ago about Kuar 1331. Ugam Lal was separate from us for the last 40 years but the business was all along joint, the profits being divided at the end of the year."

12. The income of 47,000 in respect of the business in Saran was arrived at after a full examination of the accounts and evidence produced by the Assessee in respect of his business carried on in that district. This amount did not include any sum in respect of the income made directly by the firm of Ramawater Hira Lal which carries on business at Chilwaria, but, on the other hand, it does include certain profits carried from the personal account of the Chilwaria firm in the books of account of Siwan to another personal account standing in the name of Satnarain Ramjatan who are members of the Assessee's family. These profits apparently resulted from certain transactions carried on by the Chilwaria firm through the Siwan firm and accounted for in the books of Siwan firm. It is impossible, however, to say whether in this connection there has been any overlapping or not, because the books of accounts of the Chilwaria firm have been produced neither before the Income-tax Officer, Bahraich, nor the Income-tax Officer, Saran.

13. I trust I have stated the facts of the case in sufficient detail to enable their Lordships to come to a finding on the legal questions involved.

14. I give below my opinion on the questions of law raised, as I am apparently required to do so by sub-section (3) read with sub-section (2) of section 66 of the Act.

15. The 1st question is whether the production of the order sheet to Banwari Lal by the Income-tax Officer was a proper service of a notice under section 22 (4).

16. On 7—9—1925, the Income-tax Officer recorded on the order sheet an order directing the assessee to produce the accounts of the Chilwaria firm together with the original Bijaks and Bijak Bahis on 12—9—1925. This purports to be an order under section 22 (4) and is signed on the margin by Banwari Lal. My own view of the matter, which I respectfully submit, is that for the reasons noted below, the procedure followed, in this case, is not irregular. There is no statutory form of notice under section 22 (4) and it has never been argued by the assessee that the practice followed, in this case, has, in any way, been prejudicial to him. It is true that section 63 (1) of the Act enacts that a

notice or requisition under this Act may be served on the person therein named either by post or as if it were a summons issued by a court under the Civil Procedure Code, but these directions would appear from the very wording not to be exhaustive. Further, under sub-section (2) of that section, any such notice may, in the case of a firm, be addressed to any member of the firm. Now, under sub-section (4) of section 22, the notice should be served on the person upon whom a notice has been served under sub-section (2). Person under the General Clauses Act includes an unregistered firm. The assessee in this case is an unregistered firm and Baiwari Lal is a member of that unregistered firm. It seems to me, therefore, that the correct conclusion is that, in this case, a notice under section 22-(4) has been duly served on the assessee on a proper construction of that section read with section 63 of the Act.

17. The 2nd question is whether, in view of the fact that income-tax in respect of the United Provinces firm of Ramawatar Hira Lal had been assessed at 10,000, it was any longer open to the Income-tax Officer at Saran to assess the income-tax of the Saran firm summarily under section 23 (4) because the books belonging to the Chilwaria firm had not in fact been produced. The representation of the assessee that income-tax was assessed by the Income-tax Officer, Bahraich, on a sum of 10,000 being the profit of that branch of the firm is not, in my view, a correct representation of the facts. It is true that the Income-tax Officer, Bahraich, headed his order, dated 22—10—1925 "Assessment for 1925-26". But this order is not in reality an assessment, but merely a report to the Income-tax Officer Saran, giving a history of the proceedings there and reporting what he estimates the profit of that branch to be. If it was an assessment and not merely a report of the branch income a demand notice must subsequently have been issued by him under section 29 in respect of the tax assessed on this income, but no such demand notice has been issued. Further, under section 23 (3), an Income-tax Officer is directed by order in writing after following certain procedure to assess the total income of the assessee and determine the sum payable by the assessee on the basis of such assessment, while under section 23 (4), under certain circumstances, the Income-tax Officer is directed to make "the assessment" to the best of his judgement. The assessment in this latter sub-section must have the same meaning as assessment in the previous sub-section, that is, it must mean an assessment of his total income. Further, section 64 (1) directs that where a business is carried on by an assessee in more places than one, he shall be assessed by the Income-tax Officer of the area in which his principal place of business is situate. Again, under section 64 (3), it is enacted that where any question arises as to the place of assessment, such question shall be determined by the Commissioner, or where the question is between more Provinces than one by the Commissioners concerned. This contemplates that assessment of an assessee in respect of all branches whether situated in the jurisdiction of one or more Income-tax Officers or one or more Commissioners should be made in one place and not in several. It is true that under sub-section (4), every Income-tax Officer has all the powers conferred by the Act on an Income-tax Officer in respect of income, profits or gains accruing or received within the area for which he is appointed. The object of this sub-section, as I understand, is to make co-operation between Income-tax Officers easy and to enable Income-tax Officers of areas where branch firms are situate to make necessary enquiries and report the income of the branch firm to the Income-tax Officer of the area where the principal firm is situated. It does not, in my view, imply that independent assessments should be made of the income of different branch firms by different Income-tax Officers. I am supported in this view by the finding of their Lordships the Judges of the High Court, Allahabad, in *Lachhman Das Babu Ram v. Commissioner of*

Income-tax (1). In that case, one of the points of law at issue was whether the provisions of sub-section (4) of section 64 of the Act oust the jurisdiction of the Income-tax Officer of the area in which the principal place of business is situate, so far as the assessment of the profits or gains of a branch business situate in another area and proceedings relating thereto are concerned. Their finding was that the jurisdiction of the Income-tax Officer of the principal place of business is not ousted and that under section 64 (1) of the Act, the Income-tax Officer of the principal place of business has the duty of assessing the whole of the income derived from the principal place of business as well as the various branches.

13. If I may be allowed to refer to an unofficial report I would respectfully invite their Lordships' attention to the decision of a Calcutta Bench in *Ramkishan Dass Bagri v. Commissioner of Income-tax*, (2). The question referred to their Lordships in that case was whether, when an assessment is made partly on an examination of accounts and partly on the basis of an estimate reported by another Income-tax Officer under section 64 (4) in the absence of accounts called for under section 22 (4), the assessment is to be made under section 23 (4) or under 23 (3). Their Lordships held in that case that, in the circumstances, the Income-tax Officer was entitled under section 23 (4) to make the assessment to the best of his judgment. The circumstances of that case are exactly similar to the circumstances of the case in which reference is now being made.

Manohar Lal, A. Burman and B. B. Sahay, for the Assesseees.

A. B. Mukherji and C. M. Agarwala, for the Crown.

Reference to Full Bench.

DAWSON MILLER, C. J. AND ROSS, J.:—This case comes before us on a case stated by the Commissioner of Income-tax under section 66 (3) of the Indian Income-tax, Act 1922.

The assessee was assessed under section 23 (4) of the Act on the ground that he failed to comply with a notice under section 22 (4).

The questions for decision are: (1) whether the assessee was properly served under section 22 (4); and (2) whether seeing that the income-tax in respect of the United Provinces firm of Ramawatar Hira Lal had already been assessed at Rs. 10,000, it was any longer open to the Income-tax Officer, Saran, to assess the income-tax of the Saran firm summarily under section 23 (4), because the books belonging to the Chilwaria firm had not in fact been produced.

The facts which appear from the case stated and the documents attached are shortly as follows. The firm of Ramkhelawan Sahu Ugam Lal carries on business at Siwan in the Saran District of this province. The partners in that firm are Ramkhelawan, his sons and grandsons and the sons and grandsons of his deceased brother Raj Kumar. There is also a firm at Pachruki in the District of Saran admittedly belonging to the same partners and carrying on business under the name of Mathura Prasad Sitaram, Mathura Prasad being a son of Ramkhelawan and Sitaram being a son of Raj Kumar. There is a third firm known as Ramavater Hiralal carrying on business at Chilwaria in the Baraich District of the United Provinces. All these firms belong to the same partnership. On the 6th of August 1925 in response to a notice issued under section 22 (2) of the Act a return of income was made in the name of the firm of Ramkhelawan Sahu Ugam Lal for the year 1925-26 based on the income of the

(1) 2 I. T. C. 35.

(2) 2 I. T. C. 324.

previous year. This return related to the income of the two firms in this province. On examination of the books of the firms in this province which were called for and produced, it transpired that there was a third firm at Chilwaria belonging to the same persons and on the 7th of September 1925 an order was passed and entered in the order-sheet directing the assessee to produce the accounts of that firm with original bijaks and bijak bahi on the 12th of September. This order was shown at the time to Banwari Lal, son of Ramkhelawan one of the partners who had been attending the Income-tax Officer's office from time to time on behalf of the firm in connection with the assessment. By way of acknowledging that he had received notice, he signed his name in the margin of the order-sheet opposite the order. On the 12th of September Banwari Lal attended the office again in the afternoon but did not produce the books asked for and the matter was adjourned to the following day. On the 13th of September the assessee's gumastha attended but did not produce the books required, stating that they had been written for to Chilwaria and he said that he could produce them after the Puja holidays. He was then given time until the 9th of October to produce the account books and bijak bahis and warned that if they were not produced on that date the firm would be assessed under section 23 (4) of the Act. In the meantime, namely, the 28th of September, the Chilwaria firm of Ramawatar Hira Lal made a return of the income of that firm to the Income-tax Officer of Baraich in the United Provinces and that firm was served with notice to produce its accounts on the 8th of October. On that date the firm's gumashta appeared and stated that the accounts were at Siwan in Saran and asked for a later date.

The 22nd of October was then fixed to produce the books before the Income-tax Officer of Baraich. On the following day, the 9th of October, the day fixed for the production of the books before the Income-tax Officer of Saran, Banwari Lal appeared and said that he could not produce the Chilwaria accounts as they had been required by the Income-tax Officer of Baraich in the United Provinces on the previous day. From this it appears that the firm at Chilwaria excused themselves for not producing the books in Baraich on the ground that they were in Saran whilst Banwari Lal in Saran failed to produce them on the ground that they were wanted in Baraich. On the 22nd of October, the day fixed for the production of the books in Baraich, the firm's gumashta again appeared there and stated on oath that the books were with the owners at their house in this province. Then followed communications between the two Income-tax Officers of Saran and Baraich. On the 22nd of October the Income-tax Officer of Baraich reported to the Income-tax Officer of Saran as follows:—"I am not prepared to allow him (the gumashta) any further extension and as the books are stated to be at the proprietor's head-quarters where the assessment is made, I report the whole case as it stands before me to the Income-tax Officer, Saran, who can send for the books there..... I estimate the profit of the firm at Chilwaria during the last year to be about Rs. 10,000". On receipt of this report the Officer of Saran waited until the 21st of January 1926 and, as no accounts were produced, he made an assessment on that day under section 23 (4) in respect of the income from the business both in Saran and Baraich the amount of profits being taken for the Baraich business at Rs. 10,000 as estimated by the Income-tax Officer there. The income derived from the Saran business was assessed from an examination of the accounts and evidence relating to that business at Rs. 47,000

On the first question it was urged that the service of notice on Banwari Lal on the 7th of September 1925 by showing him the order-sheet and obtaining

his signature was not proper service under section 22 (4). No special form of notice under the sub-section is prescribed by the Act, but it is provided in section 63 that a notice or requisition under the Act may be served by post, or as if it were a summons issued by a Court under the Code of Civil Procedure. In the case of a firm or Hindu undivided family the notice may be addressed to any member of the firm or any adult male member of the family. In our opinion the mode of service mentioned in section 63 is permissive and not exhaustive and there is no substance in the objection taken on the ground of improper service of notice. The notice was accepted by a member of the firm and he waived, if it were necessary, any more formal notice and did in fact appear on the day named therein. As the books were not produced the case was adjourned to the following day and on that day the excuse given was that the books were required elsewhere. Again time was given to the 9th of October with a warning that if the books were not produced assessment would take place under section 23 (4). On the 9th the same excuse was put forward that the books were required at Baraich although at Baraich on the previous day the excuse for non-production was that the accounts were with the proprietors in this province. It is clear therefore that the assessee was well aware of what was wanted from him and that he had, and had accepted, notice to produce his accounts.

Then it was said that the notice was bad because such notice could only be given before the assessee furnished his return of income, whereas in this case the return of income had been furnished on the 6th August 1925 while the notice was not issued until the 7th of September. Reliance was placed on the decision of this Court in *Brij Raj Rang Lal v. Commissioner of Income-tax* (1). The decision however has been dissented from by the Allahabad High Court in *Chandrasen Jaini v. Commissioner of Income-tax*, (2). The ground of the decision in this Court is that the words "or having made a return" in section 23 (4) would be quite unnecessary if they were not intended to be in sharp antithesis to the preceding words and to show that in the view of the legislature a notice under section 22 (4) concerns only the stage before the filing of a return. Now it is to be observed in the first place that section 22 (4) does not limit the time or define the stage at which the Income-tax Officer may serve a notice requiring the production of accounts or documents. The clause is free from any restriction except this that in the case of a person other than the principal Office of a Company notice under section 22 (2) shall have been served on him. Secondly, the object of the clause clearly is that the Income-tax Officer may have full access to the accounts and documents of the assessee and it is obvious that if this power is restrained (except as limited in the proviso), it will be difficult, if not impossible, in many cases to have a reliable and just assessment made. Thirdly, the stage at which the production of the accounts and documents will normally be required is after the return has been furnished. Before the return an Income-tax Officer can have little object in calling for accounts, and indeed if he did so, he would deprive the assessee of the materials for the preparation of his return. When the return has been furnished, the Income-tax Officer must form an opinion whether it is such a return as may be accepted as correct and complete so as to form the basis of an assessment [section 23-(1)] or whether it is incorrect and incomplete so as require support from evidence [section 23-(2)] and it is for this purpose in the main that we apprehend that the accounts are required. Fourthly it does not seem necessary to construe the words "or having made a return" in section 23 (4) by the aid of any supposed antithesis. They seem only to indicate, somewhat unnecessarily it may be, that

(1) 2 I. T. C. 453.

(2) 8 I. T. C. 17.

it is only after the return has been made that notice under section 22 (2) can issue and the assessee be required either to attend the Income-tax Officer's office or to produce or cause to be produced the evidence on which he may rely. For these reasons we differ from the decision in *Brij Raj Rang Lal v. Commissioner of Income-tax*(1), and are of opinion that the notice in this case, even though given after the return has been furnished was a good notice.

The second question may be shortly disposed of. While it is doubtless contrary to the provisions of section 64 that two simultaneous assessments should be made at different places upon the same person, it is clear that in the present case there was no double assessment. The Income-tax Officer at Baraich did not in fact assess the firm in Chilwaria; he merely framed an estimate of the profits and sent that estimate to the Income-tax Officer at Saran. There was therefore no obstacle in the way of an assessment being made by the Income-tax Officer at Saran and the procedure adopted was in conformity with the provisions of section 64.

With regard to the assessment actually made it is true that as to Rs. 47,000. the profits of the business in this province, it was based upon the return of the assessee, while only as to Rs. 10,000 was the assessment made under section 23 (4). But the assessment was one, and as the full accounts of the assessee were not produced as required, it seems to us that the whole assessment must be taken to have been made under section 23 (4) and to be unappealable.

But as this decision depends upon a view of the law which differs from that taken by a Division Bench of this Court in previous decision, the case must be referred for decision by a Full Bench.

The question which we refer for decision is whether the case of *Brij Raj Rang Lal v. Commissioner of Income-tax*,(1) was rightly decided.

JUDGMENT.*

This is a reference by the late Chief Justice Sir Dawson Miller and Mr. Justice Ross arising out of an income-tax matter. The terms of reference are "Whether the case of *Brij Raj Rang Lal v. Commissioner of Income-tax*, was rightly decided."

The facts which it is necessary to state for the disposal of this question are brief. The assessee received notice on the 15th April 1925 under section 22 (2) of the Income-tax Act, 1922, asking him to make a return as to the profits of his business and on the 6th August 1925 he received a further notice under section 22 (4) and 23 (2), the first asking him to produce books and the second asking him for certain evidence under the sub-section which I have mentioned. On the 21st August in compliance with the notice under section 22 (4) the assessee produced his books of account. On the 6th September the Income-tax Officer made an order in his order-sheet which raises the question which is debated in this case. The order runs:—

"Accounts examined. There are many disclosures. The account need be checked again with Pachrukhi account and the Chilhawaria account which latter was not produced. It is found that he has a business in grains, etc., at

(1) 2 I. T. C. 458.

* Delivered by Wort J.

Chilhawaria, where the firm goes by the name of Ramwater Hiralal. He is directed to bring the account with original bijaks and bijak Bahi on the 12th September, 1925''.

On the 21st January 1926 the assessee was assessed summarily under section 23 (4). It is argued that this was illegal as there was no power in the Income-tax Officer to issue a notice under section 22 (4) in the circumstances.

It was established in the case which was argued before the late Chief Justice and Mr. Justice Ross that on the order-sheet under that date the assessee put his initials as having received notice of the direction by the Income-tax Officer to produce the books according to the order. One question raised in argument by the learned Counsel on behalf of the assessee was that although it has been decided that as a fact notice was served on the assessee, there was no notice which sufficiently complied with the Income-tax Act, and it is argued that in spite of the decision of fact it is still open to the assessee to argue that he has received no notice. In our judgment there is no substance in that point. First of all we have the decision of fact that he has received notice and secondly as the Income-tax Act of 1922 makes no provision as to the form of notice it seems to us that the point now taken on that is unarguable and in our judgment must be decided against the assessee. The remainder of this judgment, therefore, must proceed on the basis that in fact on the 6th or 7th September 1925, the assessee received a notice under section 22 (4) and section 23 (2).

The main substance of the argument addressed to us is first of all that the notice contemplated by section 22 (4) is a notice which can be served only before a return has been made under the earlier part of the section. Taking the section by itself there seems to us to be no basis for that argument, but the point which is raised is that taking section 22 with section 23 it is clear that the notice which is contemplated by section 22-(3) can be served only before the return has been made. But dealing first of all with the construction of section 22 by itself. It provides:—“(4) The Income-tax Officer may serve on the principal officer of any company or on any person upon whom a notice has been served under sub-section (2) a notice requiring him, on a date to be therein specified, to produce, or cause to be produced, such accounts or documents as the Income-tax Officer may require.”

The condition precedent entitling the Officer to serve that notice is clearly that a notice has been served under sub-section (2) of section 22 and to suggest that there is any restriction as to the time when it may be served appears to us to be an entirely artificial construction of the section. As has already been stated there is one condition precedent and if that is complied with the section, construing it by itself, is sufficiently complied with.

But the argument which is addressed to us more particularly depends upon the construction of sub-section (4) of section 23. The argument can be best stated by the words of the judgment in the case which is referred to us, the judgment of Mr. Justice Mullick in *Brij Raj Rang Lal v. Commissioner of Income-tax*(1). He states in the course of his judgment: “The words ‘or having made a return’ would be quite unnecessary if they were not intended to be in sharp antithesis to the preceding words and to show that in the view of the legislature a notice under section 22 (4) concerns only the stage before the filing of a return.” Section 23 (4) provides that “If the principal officer of any company or any other person fails to make a return” and then it gives

the circumstances under section 22 (2) (which deals of course with a demand by the officer for a return) "or fails to comply with all the terms of a notice issued under sub-section (4) of the same section" (that is, the notice to which we have already referred, the demand by the officer for accounts and documents) and then comes the clause in the section upon which most of the argument addressed to us has been based: "Or, having made a return, fails to comply with all the terms of a notice issued under sub-section (2) of this section". The argument in fact is that sub-section (4) of section 23 is to be divided into two parts, the first division applying to the state of affairs when a return has not been made and the second applying to the case when in fact a return has been made. But there are clearly three cases contemplated by the sub-section and the words 'having made a return' are descriptive of the third class provided for by sub-section (2) of section 23. The argument is met by the judgment of the Chief Justice of Bengal in *Harmukhrai Dulichand v. The Commissioner of Income-tax, Bengal*.⁽¹⁾ In the course of his judgment he says:—"In my judgment the exposition which the Commissioner of Income-tax has given is correct. He points out that the sub-section contemplates three distinct cases and, to my mind, it is abundantly shown by him that there is no warrant in the statute for saying that after a return is made the power given by clause (4) of section 22 is gone. The only ground which I have discovered for that opinion is the insertion of the harmless words 'having made a return' into clause (4) of section 23. It seems paradoxical and improbable that the making of a return should put an end to the power of the Income-tax Officer." That appears to be a complete answer to the argument that once having made a return in compliance with the earlier part of sub-section (2) then the power which is given by the legislature to the officer under sub-section (4) is gone. As has been pointed out in the course of the argument that would lead to this drastic state of affairs; an officer may issue a notice under sub-section (4) having already issued a notice to make a return under the earlier part of the section; he might state a date for the compliance with the notice under sub-section (4) which was earlier than the date for compliance with the making of the return under the earlier part of the section. If the argument is right then the result would be that as a result of the failure to comply with the notice requiring the production of books although that was at an earlier date than the necessity to comply with the notice make a return, yet he might forthwith assess the assessee summarily although in fact the return had not been made. That is the very evil the assessee wishes to avoid. That is reducing the argument to an absurdity and a construction of that nature would seem to us to be quite unwarranted by the terms of the section. Books of account were produced on 21st August, 1925, and the order of 6/7th September demanded the production of the Chilhawaria branch; and another aspect of the same argument is that when once the Income-tax Officer serves a notice under section 22 (4) the enquiry assumes a judicial character and his power under section 23 (4) ceases and he is limited to requiring evidence on particular points, and in any event he could not under the order of 6/7th September demand further accounts. We see nothing in the Act to warrant the view that any of the powers under the Act cease before the assessment has been finally made.

The other point which has been raised is that, even supposing there was a notice under section 22 (4), no mention was made in that notice of the section or sections under which the notice was served and in consequence the assessee is in a difficult position or is penalised; in the case of non-compliance

(1) 3 I. T. C. 198.

with one section, although the right of appeal remains, non-compliance with the notice under the other section does away with the right of appeal. There seems to us to be no basis for this argument for the simple reason that nowhere in the Act is there any provision making it necessary for the officer serving the notice to state the section under which the notice is served, or to state the section under which his powers have been granted. There appears therefore to be no substance in that point either.

That being so it must be stated that, in our opinion, in so far as the case of *Brij Raj Rang Lal v. Commissioner of Income-tax*(1) was a decision on the construction of section 22 (4) it was wrongly decided. In these circumstances the Income-tax Commissioner is entitled to his costs in this Court and before the late Chief Justice and Mr. Justice Ross. Hearing fee Rs. 500.

(255) IN THE HIGH COURT OF JUDICATURE AT RANGOON.

[20th June 1928.]

Before Mr. Justice Pratt, Officiating Chief Justice, Mr. Justice Cunliffe and Mr. Justice Ormiston.

Phra Phraison Salarak

.. Assessee.*

v.

The Commissioner of Income-tax, Burma

.. Referring Officer.

Income-tax Act (XI of 1922), Sec. 7—Siamese Forest Officer residing at Moulmein—Collection of royalties there on Siamese forest timber—Salary paid at Bangkok, assessability of.

The salary paid in Bangkok by the Siamese Government to its Forest Officer residing at Moulmein and collecting there royalties on timber extracted from Siamese forests and floated down to Moulmein is not income accruing or arising in British India within the meaning of Sec. 4 of the Income-tax Act.

Case (Misc. Reference No. 2 of 1928) stated under section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Burma for the opinion of the High Court.

CASE.

This reference is made under the provisions of section 66-(2) of the Indian Income-tax Act, 1922, on the application of Mr. Phra Phraison Salarak of Moulmein in connection with his assessment to income-tax for the year 1927-28. The questions which I have been asked to refer to the High Court and which are set out in the following paragraph arise from the appellate order, dated the 18th November 1927, of the Assistant Commissioner of Income-tax for the Amherst District in which the assessment in question was confirmed.

2. The facts of the case are as follows:—

Mr. Phra Phraison Salarak is a Forest Officer in the service of the Siamese Government. He resides and functions at Moulmein in British terri-

(1) 2 I. T. C. 458.

* (1929) 1 L. R. 6 Rang. 598, A. I. R. (1929) Rang. 1.

tory. His work consists in collecting at Moulmein royalties on timber extracted from forests in Siamese territory. The cut timber is transported by streams, the earlier part of whose courses is in Siamese territory and the lower part in Burma. The logs are collected near Moulmein and by a private arrangement the firms pay in Moulmein the royalty due to the Siamese Government. Mr. Phra Phraison Salarak, the officer who collects the dues on behalf of the Siamese Government, received during the previous year a total salary of Rs. 8,754 being at the rate of 600 ticals per mensem. This amount was paid to the credit of the applicant in Bangkok. Of the total amount a sum of Rs. 8,267 was remitted to British India. The Income-tax Officer, Moulmein, determined for the purposes of the assessment to income-tax for 1927-28 the total income of the previous year as Rs. 9,234, i.e., the total amount of the applicant's salary for the year Rs. 8,754 plus Rs. 480 the value of the rent free quarters enjoyed by him. The amount was assessed under the head "Salaries". The applicant appealed against the assessment on two grounds material to the present application. He denied that the salary paid to him was "Salary" for the purposes of section 7 of the Indian Income-tax Act 1922. His second ground was that the salary was not liable to assessment as it did not arise or accrue in British India. The Assistant Commissioner decided the appeal against the applicant on both points, whereon the applicant made the present application to me.

3. The two questions which I was asked to refer are as follows:—

- (1) That the income is not salary within the meaning of section 7 (1) of the Act, since the Siamese Government cannot be regarded as the "Government" or as a public body or association or a private employer.
- (2) That, in any case, whatever may be the classification of the income, for the purpose of section 6, such income cannot be said to "accrue or arise in British India" within the meaning of section 4 of the Act.

4. As regards the first question, the assessee's contention is, in my opinion, correct. A foreign Government is clearly not one of the classes of employers specified in section 7 (1) of the Act. Therefore, I do not think that the remuneration in question can be classified as "Salaries". This question was therefore decided in the applicant's favour and does not form part of the present reference.

5. As regards the second question, the position is this. Mr. Phra Phraison Salarak resides and works in British India. For the work performed in British India he receives a certain remuneration. It is immaterial for the purpose of taxation whether or not this sum is drawn by him in British India. Section 4 (1) of the Income-tax Act makes liable to Indian income-tax *inter alia* all income, profits and gains accruing or arising in British India. To be liable to tax, therefore, it must be shown that the income in question accrued or arose in British India. There is no definition of the terms "accrue" and "arise" in the Indian Income-tax Act. But surely the plain meaning of the words "accrue and arise" as applied to a salary-earner appears to be that the salary accrues and arises in the place where he does the work.

Furthermore the meaning of the terms has been discussed in different connections in the Indian cases cited in the margin(2). A study of these judgments will show that the generally accepted interpretation of the terms in

question is to make them equivalent to "earned in" or "derived from" British India. The income in question is clearly earned by the assessee in British India where he works and resides. It therefore accrues in British India and is taxable.

The Judicial Committee of the Privy Council in the Australian case *Commissioner of Taxation v. Kirk*(1) held that as regards business the profits from any profit-earning operations accrued in the place in which these operations were carried on, although sales took place and the profits were actually received elsewhere. In conformity with this ruling salary would accrue in the place in which the services in consideration for which the salary was paid were performed, irrespective of the place where the salary is paid. In the present instance, the services were performed entirely within British India.

As regards the intention of the legislature to tax "Salaries" (in the unrestricted sense of the term earned in British India but paid out of India) section 18 (2A) inserted by clause 2 of Act XVI of 1925 removes all doubt in the matter. This provision was inserted to legalise deduction at source of income-tax payable on sterling overseas pay drawn by Government officers in the United Kingdom. In providing for deduction at source the legislature clearly assumed the income to be liable to tax under section 4 (1) of the Act.

Accordingly the answer to the question should, in my opinion, be that the income in question is income accruing or arising in British India and therefore taxable.

As regards classification it comes under the head "Other sources [section 6 (vi) read with section 12].

Daniel, for the assessee.

Eggar, for the Crown.

JUDGMENT.

PRATT, OFFG., C. J. :—I have had the advantage of reading my brother Ormiston's judgment and I concur in his proposed answer to the reference.

We are asked to decide whether salary paid in Bangkok by the Siamese Government to the credit of a Siamese Forest Officer, who collected at Moulmein royalties on timber extracted from Siamese forests and floated down to Moulmein, is income accruing or arising in British India within the meaning of section 4 of the Income-tax Act.

The Officer in question resides in Moulmein, presumably for the purposes of his work of collecting royalties.

We are not asked to decide whether the income is "salary" within the meaning of section 7 (1) of the Act, nor whether the portion of the pay remitted from Bangkok to Mr. Salarak in Moulmein can be said to be "received" within the meaning of section 4 (1).

It has been argued by the Government Advocate that for the purposes of the present reference the words "accruing and arising" must be construed as equivalent to "earned"

None of the cases cited is an authority for this contention. Had the Legislature intended to include income earned in British India within the mean-

(1) *L. R. (1900) A. C. 588.*

ing of income "accruing or arising" there, it would have been perfectly simple to say so.

I do not consider salary paid in Siam to a Siamese Official for services rendered in Burma can under the circumstances be regarded as income arising or accruing in British India.

The respondent will be allowed the costs of the reference.

Advocates fee seven gold mohurs.

ORMISTON, J.*:—This is a reference under section 66 (2) of the Indian Income-tax Act, 1922, on the application of one Phra Phraison Salarak, a Forest Officer in the service of the Siamese Government, stationed at Moulmein, where he collects the royalty on timber, extracted from forests in Siamese territory, whence it is floated down streams, the earlier of whose courses is in that territory. For his services he receives remuneration which is paid to his credit in Bangkok. He was assessed to income-tax under the head of "salary" for the year 1927-28 in respect of the total amount so paid to his credit and of the value of the rent free quarters enjoyed by him. He appealed against the assessment on the grounds, first, that the salary paid to him was not "salary" for the purposes of section 7 of the Act, and, secondly, that it was not liable to assessment as it did not arise or accrue in British India. The Assistant Commissioner decided the appeal against him on both points, whereupon he asked the Commissioner to refer to the Court the following questions:—

(1) That the income is not salary within the meaning of section 7 (1) of the Act, since the Siamese Government cannot be regarded as the "Government or as a public body or association or a private employer."

(2) That, in any case, whatever may be the classification of the income for the purposes of section 6, such income cannot be said to "accrue or arise in British India" within the meaning of section 4 of the Act.

The Commissioner was of the opinion that the remuneration of the applicant could not be classified as "salaries", and, therefore, referred only the second question.

By section 4 (1), save as thereafter provided, the Act is to apply to all income, profits or gains, as described or comprised in section 6, from whatever source derived, accruing, or arising, or received in British India, or deemed under the provisions of the Act to accrue, arise, or to be received in British India. Under section 6, save as otherwise provided by the Act, six heads of income, profits and gains are to be chargeable to income-tax. The first of these heads is "salaries" and the sixth is "other sources". The Commissioner, having held that the remuneration in question cannot be classified under the first head, classified it under the sixth head.

The question is as to whether the remuneration "accrues, or arises" in British India. The Commissioner is of the opinion that the remuneration accrues or arises in the place where the work is done in respect of which the remuneration is given, and that, consequently, the work having been done in British India, the remuneration is attracted by section 6. The Government Advocate has supported this view. The expression is not defined in the Act, and no authority directly bearing on the point now to be decided has been

quoted. Reference, however, has been made to a number of authorities where the expression has been discussed, and it is suggested that as a result it should be interpreted as meaning "earned in" or "derived from".

In *Board of Revenue Madras v. Ramanadham Chetty*(1) it was held under section 3 (1) of the Act of 1918, the wording of which is similar to that of section 4 (1) of the present Act, that a resident in British India is not liable to tax in respect of the income of a business carried on outside British India, where such income is not remitted to British India. The case itself is not in point, and the only passages in the report to which the Government Advocate has directed attention are a discussion by Abdur Rahim, Offg. C. J., (on page 42) on a possible difference between the phrases "accrues and arises" and "accrues or arises", and quotations by Oldfield, J., (on page 43) from dictionaries as to the meaning of the word "accrue". From these it appears that the primary meanings are "to arise or spring as a natural growth or result", "to come by way of increase" and "to grow or arise"; while as secondary meanings it has "to become a present and enforceable right", and "to become a present right of demand".

Seshagiri Avvar, J., (at page 46) quotes some further definitions. In Murray's Oxford Dictionary the words "accrues" and "arises" are regarded as synonymous. In the Century Dictionary the word "accrue" is defined to mean "to become a present or enforceable right to demand." Stroud defines "arising in the United Kingdom" as "coming into the person's hands in the United Kingdom."

In *Rogers Pyatt Shellac & Company v. Secretary of State*(2) Mukerji, J., after discussing theoretical distinctions between "accruing" and "arising" arrives at the conclusion that the words denote the same idea, or ideas very similar, and that both words are used in contradistinction to the word "receive" and indicate a right to receive. They represent, he says, a stage anterior to the point of time when the income becomes receivable and connote a character of the income which is more or less inchoate. These definitions do not support the view that income accrues or arises in a particular country by reason of the fact that it is "earned" in that country. On the contrary they go to show that income "accrues" and "arises" in the country where there is a right to demand payment of it, or where, in fact, it is paid. In the case referred the applicant is a Siamese Government servant and there is nothing to indicate that he has a right to demand payment of his income in Moulmein, and, according to the case, it is actually paid in Bangkok.

Commissioners of Taxation v. Kirk(3) was a decision of the Privy Council on a New South Wales Act which imposed income-tax on incomes *inter alia* (1) "accruing or arising to any person wheresoever residing from any profession, trade, employment or vocation carried on in New South Wales",.....(3) "derived from lands of the Crown held under lease or license issued by or on behalf of the Crown" and (4) "arising or accruing to any person wheresoever residing from any kind of property" (with an immaterial exception) "or from any other source whatsoever in New South Wales not included in the preceding sub-sections". A company in part derived its income from the extraction of ore from leasehold lands held from the Crown in that Colony

(1) 1 I. T. C. 87.

(2) 1 I. T. C. 363 at page 372.

(3) L. R. (1900) A. C. 588.

and from the conversion in that Colony of the crude ore into a merchantable product. It was held that, notwithstanding that the finished products were sold exclusively outside the Colony, this income was assessable. Their Lordships said that the real question seemed to be whether any part of the profits of the company were earned or produced in the Colony. And, later in the judgment after pointing out that the word "derived" is synonymous with arising or accruing, they went on to observe that "there are four processes in the earning or production of this income:—(1) the extraction of the ore from the soils; (2) the conversion of the crude ore into a merchantable product, which is a manufacturing process; (3) the sale of the merchantable product; (4) the receipt of the moneys arising from the sale. All these processes are necessary stages which terminate in money, and the income is the money resulting less the expenses attendant on all the stages. The first process seems to their Lordships clearly within sub-section (3), and the second or manufacturing process, if not within the meaning of 'trade' in sub-section 1 is certainly included in the words 'any other source whatever in sub-section (4)'."

Their Lordships' view, therefore, was that it is the source of the income which has to be considered, and not the place where it is received.

This case was referred to in *In re: Aurangabad Mills, Limited*(1), a decision under section 3 (1) of the Act of 1918. It was there held that the profits of a company which are made from manufacture carried on beyond British India cannot be said to accrue or arise in British India on account of the head office being in Bombay, where also the directors control the business. Macleod, C. J., (at page 119), after quoting the above cited passage from the judgment of their Lordships remarked that the doubt which might have arisen in *Commissioners of Taxation v. Kirk*(6) whether the profits were not derived at a place where the third and fourth processes were carried out, did not arise in the case before him because all the four processes were carried out in Hyderabad. This case was followed in *Board of Revenue v. Ripon Press*(2). In *Commissioner of Income-Tax, Burma v. Messrs Steel Brothers & Co., Ltd.*(3) it was held, applying the principles laid down in *Commissioners of Taxation v. Kirk*(6), that in determining whether any income, profits or gains arise or accrue "we must not be content to look at the last stage of the accrual, but must take into consideration the previous stages as well". The company was non-resident in British India, but at mills situate in Burma it worked up commodities and materials into forms suitable for use and shipped them to the United Kingdom where they were sold. It was held that the profits or gains accruing to the company in respect of this business must be deemed (within section 42 (1) of the Act) to be income accruing or arising within British India.

Sunder Das v. Collector of Gujrat(4) and *Sir Saiyid Ali Imam v. the Crown*(5) have been cited. These cases deal with the meaning of the expression "received in British India", which is not part of the reference in this case, and need not be discussed.

Reference has been made by the Government Advocate to sections 42 (1) and 18 (2-A) of the Indian Income-tax Act, 1922. Section 42 (1) provides that in the case of a non-resident, all profits or gains accruing to him through or from any business connection or property in British India is to be deemed to

(1) 1 T. C. 116.

(2) 1 I. T. C. 202.

(3) 2 I. T. C. 119.

(4) 1 I. T. C. 189.

(5) 1 I. T. C. 402.

(6) L. R. (1900) A. C. 588.

be income accruing or arising within British India. The effect of section 18 (2-A), which was inserted by Act XVI of 1925, is to render subject to income-tax any income chargeable under the head "salaries" which is payable to the assessee out of India by or on behalf of Government. These sections do not appear to be of assistance in the general construction of the words "accruing" and "arising" in section 4 (1). They seem to be designed to bring within the ambit of the tax special classes of cases which would otherwise escape. I am unable to appreciate the argument to be found in the reference which is based on the position of a salary earner. It is said that in his case the salary accrues and arises in the place where he does the work, which is in British India, and that it therefore accrues in British India and is taxable. But this argument overlooks the fact that the Commissioner has expressly held that the remuneration of the assessee is not "salary" and has classified it under "other sources".

If the correct principle be that the words accrue and arise when applied to income are to be governed by the source from which the income accrues and arises, it would appear that in the case referred that source is to be found in Bangkok rather than in Moulmein. The assessee is a Forest Officer in the service of the Siamese Government. It is not stated that his remuneration is in the nature of a commission on the amount of revenue collected. On the contrary it is said to be 600 ticals per mensem. The inference to be drawn is that he would get his remuneration *qua* Forest Officer, whether he worked in Moulmein collecting royalty, or whether he worked in Siam in that or any other capacity. From this point of view his remuneration accrues and arises in Bangkok where it is payable and is in fact paid. If on the other hand we are to have regard to the definition of the words, the only place where it would seem that there is a present and enforceable right on the part of the assessee to demand the remuneration and where it comes into his hand, is also Bangkok.

In conclusion I may refer to the observation of Sir Shadi Lal, C. J., in *Sandar Das v. Collector of Gujrat* (1) after citing the rule of interpretation applying to fiscal enactments, that "It is a sound principle that the subject is not to be taxed without clear words to that effect; and that *in dubio*, you are always to lean against the construction which imposes a burden on the subject." The Government Advocate expressed the view that the Legislature had advisedly refrained from defining the terms accruing and arising. In my view the meaning of the terms, as applied to the facts of the case, is as above stated and is perfectly plain. If, on the other hand, the meaning is ambiguous, the sound principle enunciated by Sir Shadi Lal is applicable and it ought to be applied.

I would answer the question referred by saying that the income, the subject matter of the reference, cannot be said to "accrue or arise" in British India within the meaning of section 4 of the Indian Income-tax Act, 1922.

CUNLIFFE, J.:—I also concur. The scope of this reference has been very much narrowed. The Commissioner has satisfied himself of the answer to the first proposition put forward by the respondent. In that regard the Commissioner holds the view that the respondent's income does not come under the head of "Salary" within the meaning of section 6 of the Act. Nor did the respondent (very wisely, I think) suggest to the Commissioner that he should ask the opinion of the Court as to whether the emolument which he (the respondent) is paid by the Siamese Government is received in British India. All we have to do here is to decide, as my brother Ormiston has pointed out, whether such emolument accrues or arises in British India. It has been held on

several occasions that there is no difference between the two words "profits" or "gains" which are used in the section we are considering. I am inclined to think that there is no real difference in law between the words "accruing" and "arising". Some authorities have thought that the word "accrue" suggests a periodical right to money and the word "arise" suggests only a single right or possibly the beginning of a periodical right. But these views seem to me to be refinements and over-refinements of the language of the statute. To my mind, the double expression "accruing and arising" connotes the source from which the right to obtain money springs. Undoubtedly the source here was in the Kingdom of Siam, remuneration from the Siamese Government to one of the officers of their Forest Service. In my view, too, the expression "accruing or arising" is used in contradistinction to the word "received", but, as I have pointed out, we are not considering the question of where the money was actually received, or to what place it was remitted after its receipt which may be the same thing in law as "received". It was very strongly urged upon us that the real meaning of "accruing" and "arising" as applied to the income of the respondent was to be found in the place where the income was earned; but, for the reason mentioned above, I do not agree with that view.

(256) IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Mr. Justice Mukerji and Mr. Justice King.

(2nd July 1928)

The Swadeshi Cotton Mills Co., Ltd., Cawnpore .. Assessee.*

vs.

The Commissioner of Income-tax, United Provinces .. Referring Officer.

Income-tax Act (XI of 1922), Sec. 10 (2) (vii)—Engine found obsolete in 1923—Sale in 1926 on its breaking down and replacement by another engine—Obsolescence allowance, claim for.

Where a steam driven engine found in 1923 to require replacement as having become obsolete was discarded and sold in September 1926, when it broke down beyond repairs and was replaced by an electrically driven engine

HELD, that the sale was in consequence of its having become obsolete within the meaning of Sec. 10 (2) (vii) of the Income-tax Act.

Case (Misc. Reference No. 231 of 1928), stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, United Provinces, for the opinion of the High Court.

CASE.

The Swadeshi Cotton Mills Company, Limited, Cawnpore, was assessed to income-tax and super-tax in the current financial year on July 30, 1927.

* (1928) 26 A. L. J. 1319 A. I. R. (1929) All- 70.

2. The assessee claimed "obsolescence allowance" amounting to Rs. 49,988 in respect of an engine, but the Income-tax Officer disallowed the claim in the following terms:—"Engine break-down. The assessee has debited Rs. 1,01,096 for repairs and renewals to spinning account and Rs. 8,015 to weaving account. Details have been furnished in schedule No. 7 sent with the return. A sum of Rs. 53,398 on account of break-down of an engine is included in this. Last year there was an accident in the mill and the engine broke down and the assessee replaced it by electric motors and transformers, the purchase of which is debited to repairs and renewals account. Evidently this item is of capital expenditure, and loss by break-down of an engine is a loss of capital nature and cannot be debited to revenue account. The assessee in his letter, dated July 26, 1927, says that loss may be allowed under the 'obsolescence' clause. This case is similar to one decided by the Hon'ble High Court of Judicature of Madras in *Ratan Singh v. Commissioner of Income-tax, Madras*(1). The loss incurred by destruction of a machine cannot be claimed as 'obsolescence allowance'. This loss, therefore, cannot be allowed. On looking into the details of Rs. 53,398 it was found that a sum amounting to Rs. 3,399-15-3 consisted of items which ought to have been debited to current repairs and renewals accounts. Deducting this item, there remains a sum of Rs. 49,988 which is disallowed."

3. The assessee appealed to the Assistant Commissioner of Income-tax who directed a further enquiry for the reasons given in his order of which an extract copy is attached (appendix A).^{*} Copies of the letters cited by the Assistant Commissioner of Income-tax are attached in appendix D^{*} (items I and II) so far as relevant to the present reference. The Income-tax Officer duly submitted a report of which a copy is contained in appendix B.^{*} Copies of the correspondence furnished by the company and referred to by the Income-tax Officer, together with a copy of the statement made by Mr. H. Horsman on December 14, 1927, are given in appendix D^{*} (items III to IX). The Assistant Commissioner of Income-tax rejected the claim (extract copy of order in appendix C).

4. The Company has now claimed a reference to High Court on the question of law set out in the following telegram:—"Point of law involved is as to construction of section [stop] Only requisites to found claim are that machine was obsolete and was discarded [stop] Both facts found in present case assessee cannot be deprived of allowance by intervention of accident before discard [stop] We could have repaired machine and subsequently discarded claiming cost of repairs as well as obsolescence allowance [stop] Construction of section as relied upon by Assistant Commissioner erroneous that old plant should actually have been replaced before allowance could be claimed and that condition for grant of allowance was that after replacing it should have been sold or discarded [stop] Nothing in section that claim dependent on replacement."

5. The point of law which arises and which is stated for the decision of the High Court is:—"Was the engine in question sold or discarded in consequence of its having become obsolete within the meaning of section 10 (2) (vii) of the Indian Income-tax Act 1922?"

6. The petitioner desires "to have the following question inserted to precede that as put in" the foregoing paragraph:—"Whether the fact of the

^{*} Not printed.

(1) 2 I. T. C. 107.

discarding of a machine admittedly obsolete does not constitute sufficient compliance with the provisions of section 10 (2) (vii) of the Indian Income-tax Act, 1922, to support a claim to the allowance thereunder?"

The reason assigned by the company is that "in its present form it would appear that the question (i.e. in paragraph 5) is put solely on a point of fact upon which your finding is recorded against the company." The Commissioner is unable to state the question desired by the company because it is in vague terms, and the point in issue is whether on the facts found in this case a certain allowance should be given.

7. In the opinion of the Commissioner of Income-tax the answer to the question, which is stated for the opinion of the High Court in paragraph 5, is in the negative.

Extract from Assistant Commissioner's order dated January 16, 1928.

For reasons given in my order, dated December 4, 1927, this case was remanded to the Income-tax Officer for further enquiry on the following points:— (1) that the engine which broke down was in fact obsolete, and (2) that having become obsolete it had been discarded before the break-down came.

His report, dated December 19, 1927, may be seen.

Briefly the facts are that last year by an accident in the mill the engine, for which the obsolescence allowance is claimed, broke down, and the appellants replaced it with electric motors and transformers of which they debited the cost price to the repairs and renewals account. As noted by the Income-tax Officer in his assessment note, the original cost of the engine was Rs. 1,01,066. After the break-down it was sold as scrap iron for Rs. 1,256-7-9 on March 29, 1927 (*vide* copy of a letter from Messrs. Bhagwan Das Shroff Prasad) which has been filed by the appellants before the Income-tax Officer. The appellants claim the difference between the original cost, as reduced by the aggregate depreciation allowance in previous years, and the scrap value as an obsolescence allowance.

As stated by me in my order, dated December 4, 1927, this can be allowed only if it is shown that the engine which broke down was in fact obsolete, and that having become obsolete it had been discarded before the break-down came. If it was discarded as a result of the break-down it is clear that, under section 10 of the Income-tax Act they were not entitled to any obsolescence allowance. The actual words of clause 7 make it clear that this allowance does not become due until the superseded machinery has been sold or discarded. It is admitted that it was not sold at all as a machinery but as scrap-iron, and this scrap-iron, too, was not sold until March 29, 1927, namely, until about three months after the close of the calendar year 1926, on the basis of which the accounts of the company are maintained. My reading of this clause of section 10 is that the obsolescence allowance cannot be claimed until the superseded machinery has been sold, or discarded. Owing to the break-down intervening it was, in my opinion, physically impossible for this to happen. The broken engine could not remain at work until the new machinery, temporary or permanent, had arrived. It had ceased to function because of the break-down before the installation of the temporary machinery. From the letter of Messrs. Scott and Hodgson, Limited, Manchester, dated January 13, 1923, it is fairly clear, I think, that the appellants had an intention of discarding the engine apparently because for an extended scheme of business it was inadequate, and consequently I have no difficulty in accepting the statement of Mr. Horsman, the director of the

company, that the engine was obsolete. But this is not the only condition for a title to the allowance. It should have been proved that it was discarded, not because of the accident intervening but because it had become obsolete. What I mean is that the old engine should actually have been replaced by a more up-to-date machinery before the allowance could be claimed, and the condition for the grant of the allowance itself was that after replacing it should have been sold or discarded when the difference between the depreciated value and sale proceeds or the scrap value could have been worked out. In this case it is admitted that the engine was sold as scrap-iron after the break-down some three months after the calendar year on the basis of which the present assessment has been made. Mr. Horsman urges that there was actually an intention to discard the engine long before the break down, but the actual fact of discarding was expedited by the break-down. This is only another way of showing that the intention to discard it was frustrated by the break-down which intervened. The obvious difference, therefore, is that the discarding did not take place because of the engine being obsolete but because of the break-down. The necessary condition of the superseded engine having, in the first place, been replaced was not fulfilled in this case. The appellants are not, therefore, entitled to an obsolescence allowance.

Kailas Nath Katju, for the assessee.

Uma Shankar Bajpai, for the Crown.

JUDGMENT.

This is a case stated by the Commissioner of Income-tax at the instance of the Swadeshi Cotton Mills Company, Limited, Cawnpore.

The question submitted for our answer runs as follows:—Was the engine in question sold or discarded in consequence of its having become obsolete within the meaning of section 10 (2) (vii) of the Indian Income-tax Act, 1922?

The facts are given in the order of the learned Assistant Commissioner, dated 16th January 1928 and are as follows:—

The Swadeshi Cotton Mills Company, Limited, had a steam driven engine. So far back as in 1923 it was decided that it should be replaced (at such date as might be found convenient) on the ground that it had become obsolete. The machine was, however, not actually replaced although an electricity driven engine was provided. In September 1926, the engine actually broke down and the question arose whether it should be repaired or not. Within a few days, the Company decided that it should not be repaired but should be sold. It was actually sold for Rs. 1,200 and odd. The question is whether the machinery was discarded because it was obsolete within the meaning of clause (vii), sub-section (2) section 10 of the Indian Income-tax Act.

As already stated the machine had been declared to be obsolete. It was discarded because two things happened. It was obsolete and it also broke down and it broke down past repairs. In the circumstances we are of opinion that the engine was sold in consequence of its having become obsolete within the meaning of section 10 (2) (vii) of the Indian Income-tax Act, 1922. The cost of this reference will be paid by the Government. The fee certified by Dr. Katju day, that is to say a sum of Rs. 250. The Government Advocate may file his certificate within six weeks.

(257) IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Mr. Justice Mukerjee and Mr. Justice Banerji.

(3rd July 1928).

Jhuri Misra

.. Assessee.

vs.

The Commissioner of Income-tax, United Provinces .. Referring Officer.

Income-tax Act (XI of 1922), Secs. 27 & 30—Order refusing to re-open assessment—Appeal thereon—Jurisdiction of the Appellate authority to review assessment under Sec. 23 (4).

In an appeal against an order under Sec. 27 of the Act refusing to re-open an assessment, it is not open to the Assistant Commissioner to enter into the merits of the assessment made under Sec. 23 (4) or review the same.

Case (Misc. Reference No. 421 of 1928), stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, United Provinces, for the opinion of the High Court.

CASE.

On April 9, 1927, the assessee was ordered to be served with a notice under section 22 (2) of the Income-tax Act requiring him to submit his return of income on or before May 23, 1927. This notice was duly served on the assessee on April 15, 1927.

No return of income was submitted, and on January 10, 1928, after making necessary inquiries, the Income-tax Officer made a "best judgment" assessment under section 23 (4) and issued a notice of demand which was served on the assessee on January 13, 1928.

On January 30, 1928, the assessee applied to the Income-tax Officer under section 27 for reopening the assessment on the grounds which stated briefly, are:—

- (1) That about the time the notice for the return of income was served the assessee was involved in certain notified area cases in which his property and prestige were in danger. He was so worried on account of those cases that he mislaid the form of notice and forgot all about it afterwards. There was no intention to evade compliance with the notices:
- (2) That the assessee was illiterate and could not ascertain what exactly he was required to do under the notice, and by what date:
- (3) That the assessee did not, afterwards, get any other notice so that he could come and see the Income-tax Officer and put his case before him:
- (4) That the only means of the assessee's livelihood was his village property, the business having been closed last year on account of heavy losses of which the assessee probably gave due intimation to the Income-tax Officer through his Mukhtar Am:

- (5) That without taking into consideration the fact that the assessee had closed his business the Income-tax Officer assessed him to income-tax on an abnormally high figure.

The application was presented to the Income-tax Officer personally by the assessee, who was asked to substantiate it by producing his evidence on February 10, 1928. On this date the assessee did not come but sent his Mukhtar Am who stated briefly to the effect that since the month of *Fagoon* or *Chait* (corresponding to March and April, 1927) the assessee (Jhuri Misra) was so upset over certain revenue and notified area cases which had been brought against him that he forgot to send his return of income, that the grain shop had been closed and that the only business carried on was money-lending. The assessee himself never went into the witness-box and produced no other evidence whatever. Disbelieving the statement of the assessee's Mukhtar Am the Income-tax Officer rejected the application and refused to re-open the case.

The assessee then appealed to the Assistant Commissioner, who agreeing with the Income-tax Officer dismissed the appeal.

The assessee now wishes me to refer his case to the High Court on the following points of law which are set forth by him:—

1. Whether the Income-tax Officer was justified, in contravention of the rules and instructions of the Income-tax Manual under section 23 (4), in arbitrarily assessing the petitioner and raising the tax from Rs. 250 to Rs. 1,400 without issuing any notice under section 22 (4) or 23 (2), and without summoning him under sections 37 and 38, and without pointing out to him the additional information to be used against him, and whether the Assistant Income-tax Commissioner has no jurisdiction to interfere in the matters of Income-tax Officer's proceedings under section 23 (4).
2. (a) Whether the Income-tax Officer had any jurisdiction whatsoever to make any inquiry regarding the transaction, trade and income, if any, of Bombay, the area outside his province.
- (b) Whether the Income-tax Officer could legally assess the petitioner on such an exalted amount without any instance or report from the Income-tax Officer, Bombay. Whether the Assistant Commissioner could ignore this indiscrepancy (*sic*) of the Income-tax Officer.
3. Whether the assessment as it stands is to the best of the Income-tax Officer's judgment within the meaning of section 23 (4), or it is quite arbitrary and unwarranted by law.
4. Whether in the absence of any evidence on record the Income-tax Officer was justified in assessing on the profits on grain income when its very source of income is denied.
5. Whether in non-receipt of notice under section 22 (4) or 23 (2) and the presence of the assessee in another court on the date when the return was due are sufficient causes within the meaning of section 27 of the Income-tax Act.

The assessee is entitled to have his case stated in respect of those law points only which arise in this case out of an order under section 31.

The points enumerated by the assessee are not appropriately worded, but the intention is clear.

In (5) the assessee inquires whether the facts set forth in it are "sufficient cause" within the meaning of section 27 of the Income-tax Act? But the facts are not as stated. No notice under section 22 (4) or 23 (2) was issued by the Income-tax Officer. Indeed, when no return of income was submitted the Income-tax Officer could not legally issue a notice under the latter section. As regards notice under section 22 (4), the Income-tax Officer undoubtedly has power independently altogether of the question whether a return has been filed or not. But the power is discretionary, and the discretion vested in the Income-tax Officer is not subject to appeal and is, therefore, not controllable by a higher authority. The fact that the Income-tax Officer did not issue a notice under section 22 (4) cannot, therefore, be urged as a "sufficient cause" for not submitting the return of income under section 22 (2). The Income-tax Officer was not bound to issue a notice under section 22 (4). A notice under section 22 (4) is intended mainly to secure the production of accounts. The assessment record shows that since the year 1918 the assessee never produced accounts. Indeed, on more than one occasion their very existence was denied. If, therefore, the Income-tax Officer did not issue a notice under section 22 (4), he cannot be said to have exercised his discretion improperly. Further, the question "what is sufficient cause" is primarily a question of fact and not of law; and in the circumstances of this case it is impossible to say that it has any legal aspect. The assessee, who never filed a return of income since the year 1922-23 and never the accounts so far as the records in existence show, stated last year, that is in 1927-28, in his petition under section 27 that he did not submit his return of income because he was preoccupied and in his preoccupation he forgot all about it. He did not go into the witness-box himself although the reason ascribed was an affair to which he of all others was the best person to testify. He chose to send his representative whose statement was rejected by the Income-tax Officer, and in rejecting it the Income-tax Officer was not dealing with any point of law, but with a plain question of fact whether the assessee was so preoccupied with litigation that in his embarrassment he forgot to send the return. He came to the conclusion that there was no evidence to show that he was and that on the contrary the persistent default in complying with notices showed that he was gambling on the result of the assessment.

Neither before the Income-tax Officer in the course of the disposal of the petition under section 27 nor before the Assistant Commissioner on appeal was present the issue whether in the year 1926-27 on the income of which the "best judgment" assessment was made under section 23 (4) assessee had grain business or not. The issue was a narrow one, that is, whether the appellant had sufficient cause for not complying with the notice under section 22 (2) requiring him to submit a return of income. The fourth point set forth by the assessee cannot, therefore, be said to arise out of an order under section 31, the order passed on appeal, and the assessee is not therefore entitled to have it stated.

The third point in effect amounts to a demand for a second appeal in respect of an assessment under section 23 (4) which, under the proviso to

section 30 (1) of the Act, is non-appealable and cannot be stated for the same reason as point no. 4.

Neither part (a) nor part (b) of the second point was the subject of any contention in the appeal against the Income-tax Officer's order under section 27, and the assessee is not, therefore, entitled to have it stated. The point does not arise out of the appellate order.

There are many extraneous matters introduced in the first point raised by the assessee, some of which have already been dealt with. For instance, the reference to section 23 (2) is entirely out of place in a proceeding which originated in the non-submission of the return of income. I have already dealt with the fact that the power to issue a notice under section 22 (4) is discretionary, and that the discretion is not controllable by a higher authority, and it is equally in the discretion of an Income-tax Officer to summon witnesses or enforce the production of documents or issue commission under section 37 or put the machinery of section 38 into action when a return of income has not been submitted. The procedure adopted by the Income-tax Officer does not, in any way, conflict with the instructions laid down in the Income-tax Manual which, moreover, have no statutory authority. Nor is an Income-tax Officer required by any provision of the Act to lay before an assessee the information obtained by him before making an assessment under section 23 (4). On the contrary, when a default has occurred in respect of any of the matters dealt with in clause (4) of section 23, the Income-tax Officer has no option whatever but to make an assessment to the best of his judgment; and in forming his judgment he is at liberty to utilize any information that comes to his notice, and there is no appeal against a judgment formed in this manner. But in challenging the fact that in an appeal against an order refusing to reopen an assessment under section 27 an Assistant Commissioner has no jurisdiction to interfere with the assessment under section 23 (4) the assessee has in fact raised a point of law arising out of the proceedings under section 31 which emerges more appropriately in the following form and which I should refer for the opinion of the Hon'ble Judges of the High Court:—

In an appeal against an order refusing to re-open an assessment under section 27, is an Assistant Commissioner of Income-tax at liberty to enter into the merits of an assessment made under section 23 (4)?

Under section 66 (2) I am required to state my opinion on the point referred. The order under section 23 (4) is not appealable but can, on sufficient cause shown for non-compliance, be set aside by an Income-tax Officer on a petition under section 27. When an Income-tax Officer acting legally in the discharge of his duties rejects such a petition and refuses to re-open an assessment, the Act provides specially for an appeal against the order refusing it. I am, therefore, of opinion that such an appeal is confined to a consideration of the grounds on which the refusal was based, and that the Assistant Commissioner is not at liberty to go behind the assessment against which there is explicit provision forbidding an appeal.

JUDGMENT.

This is a statement of a case under section 66 of the Income-tax Act, 1922, made at the instance of one Jhuri Misra.

The facts are given in the statement and briefly are these:—

Jhuri Misra was served with a notice under section 22 clause (2) of the Income-tax Act and was called upon to furnish a return of his income. He did not do so. Thereupon without any further information to him a best Judgment assessment was made under section 23 (4) of the Act. Thereupon Jhuri Misra appeared before the Income-tax Officer under section 27 of the Act and informed him that there was sufficient reason which prevented him from furnishing a return. His case was that about the time when notice was served on him he was busy with other litigation which worried him very much. He himself did not appear before the Income-tax Officer but sent his agent. The agent was examined by the Income-tax Officer and was disbelieved. The Income-tax Officer was of opinion that no sufficient cause had been shown for not furnishing a return.

Jhuri Misra then went in appeal under section 30 of the Income-tax Act before the Assistant Commissioner. That Officer agreed with the Income-tax Officer that no sufficient cause for not furnishing the return has been furnished. On this ground he affirmed the order of the subordinate officer. He refused to consider the question whether the assessment of Rs. 1,400 in place of the assessment of Rs. 250 made during the earlier years was justified.

After this Jhuri Misra went with an application to the Commissioner of Income-tax and asked that either he should review the orders of his subordinate officers, or he should make a reference to the High Court. He stated several points for reference but the Commissioner accepted only one as the proper point to be referred to the High Court. Jhuri Misra did not take any steps by which other points, which he sought to raise could be brought before the High Court. We are accordingly required to answer only one question, namely:—“In an appeal against an order refusing to re-open an assessment under section 27, is an Assistant Commissioner of Income-tax at liberty to enter into the merits of an assessment made under section 23 (4).”

On this point the answer seems to be clear and to be furnished by the proviso to sub-section (1) of section 30 of the Act. There, it is clearly laid down that no appeal shall lie in respect of an assessment made under sub-section (4) of section 23, or under that sub-section read with section 27. It was not in our opinion open to the Assistant Commissioner to review the best judgment assessment made by the Income-tax Officer. We have been referred to two rulings, one of the Calcutta High Court and the other of the Lahore High Court, on points which are really not before us. We do not feel called upon to discuss them. An answer to the reference in the terms stated above will be sent to the Commissioner of Income-tax. The applicant Jhuri Misra will pay the costs of this hearing which will include Government Advocate's fee, assessed by us at Rs. 125. The Government Advocate is allowed ten days time to file the certificate of fees.

(258) IN THE HIGH COURT OF JUDICATURE AT RANGOON.

Before Sir Henry Pratt, Kt., Officiating Chief Justice and Mr. Justice Cunliffe.

(16th July 1928).

A. K. A. C. T. V. V. Chettyar

Assessee.*

vs.

The Commissioner of Income-tax, Burma

... Referring Officer.

Income-tax Act (XI of 1922) Secs. 23 (4), 27 and 30—Order rejecting application under Sec. 27—Appealability—Scope of proviso to Sec. 30.

The proviso to Sec. 30 of the Income-tax Act is no bar to an appeal against an order rejecting an application under Sec. 27, such an order not being an assessment under Sec. 23 (4) read with Sec. 27 within the meaning of the proviso.

Application (Civil Misc. Application No. 26 of 1928) under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) for an order directing the Commissioner of Income-tax, Burma, to state a case for the opinion of the High Court.

Clark and Venkataram, for the assessee.

A. Eggar (Government Advocate), for the Crown.

JUDGMENT.

This is an application for a mandamus to compel the Commissioner of Income-tax to state a case under section 66 of the Income-tax Act. The facts are set out at length in the application.

The A. K. A. Firm of Rangoon which consisted of two partners, the applicant A. K. A. C. T. V. V. Chettyar and A. K. A. C. T. A. E. Alagappa Chettiar, discontinued business in 1925 August; the assets were divided between the partners who have been since carrying on business as separate joint family firms under the styles of A. K. A. C. T. V. and A. K. C. T. A. L. respectively.

For the financial year 1925-26 notice was served on the then agent of the A. K. A. Firm on 8th April 1925 to make a return for income-tax purposes.

Applicant eventually made a return and claimed the benefit of section 25 (3) of the Income-tax Act as the firm had been dissolved.

Applicant objected to producing the books of the firm and to the proposed method of assessment. Ultimately the Income-tax Officer peremptorily settled March 31st, 1926, for the production of accounts. The accounts were not produced and the Officer made an assessment *ex-parte* against each member of the A. K. A. Firm.

* (1928) I. L. R. 6 Rang. 652; A. I. R. (1929) Rang. 8.

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Applicant appealed to the Assistant Commissioner who dismissed his appeal, and left him to apply for a fresh assessment under section 27. An application was made under section 27 but was refused. An appeal to the Commissioner of Income-tax was unsuccessful. The Commissioner was asked but declined to make a reference to this Court; hence the present application under section 66 (3) for an order to state a case on specified points of law.

A preliminary objection has been taken by the Government Advocate that the application is incompetent since no appeal lies to the Assistant Commissioner from the order refusing to make a fresh assessment under section 27.

It is contended that the proviso to section 30 that no appeal shall lie in respect of an assessment made under sub-section 4 of section 23 or under that sub-section read with section 27 precludes such an appeal, since it must be taken that the Officer having dismissed the application for a fresh assessment under section 27, there remains an assessment under sub-section (4) of section 23 read with section 27.

The contention is clearly not maintainable. There was an application for a fresh assessment under section 27 which was refused. The assessment under section 23 (4) was not cancelled. There was not therefore an assessment under section 23 (4) read with section 27 as argued. A refusal to make an assessment is not an assessment.

Section 30 definitely provides for an appeal against a refusal of an Income-tax Officer to make a fresh assessment under section 27.

What the proviso clearly means is (1) that there shall be no appeal against an assessment made under section 23 (4) and, (2) that when an assessment under section 23 (4) has been cancelled under section 27 and a fresh assessment made there shall be no appeal; that is to say, that if the assessee succeeds in his effort to obtain a fresh assessment under section 27 he shall be debarred from appealing against that fresh assessment. The assessee is not precluded from preferring the appeal against the refusal to make a fresh assessment under section 27 which is allowed in the body of section 30.

In his order rejecting the two applications for a reference to this Court under section 66 (2) on a number of questions, the Commissioner of Income-tax took the view that the only questions for decision were of pure fact, viz.:—whether applicants had a reasonable opportunity of complying with the Income-tax Officer's notice and whether there was an adequate reason for non-production of accounts. There was therefore no question of law to refer.

We consider that the only question for determination was whether applicant had sufficient cause for non-compliance with the Income-tax Officer's notices. He obviously had not and we see no reason to think the findings of fact wrong. Applicant and his quantum partner were obviously placing every obstacle in the way of a just assessment and they have only themselves to thank if the result of their efforts is, that they have been assessed in a way and under a section which they do not like.

We do not feel called upon to require the Commissioner to state a case upon any of the points raised before us.

The application is dismissed with costs. Advocate's fee five gold mohurs.

(259) IN THE COURT OF THE JUDICIAL COMMISSIONER AT NAGPUR.

*Before Mr. Hallifax, and Mr. Kinkhede,
Additional Judicial Commissioners.*

(18th July 1928).

Jainarain Motiram of Shegaon

Assessee.*

vs.

The Commissioner of Income-tax, Central Provinces .. Referring Officer.

Income-tax Act (XI of 1922), Secs. 10 (2), (ix) and 11 (2) and 66 (2) and (3)—Application to Court for reference—Jurisdiction to direct reference on questions of law not formulated before Commissioner—Adat charges incurred in account year but not paid—Claim for deduction.

An assessee is entitled to move the High Court under Sec. 66 (3) of the Income-tax Act for a direction to the Commissioner to refer questions of law to the Court though they may not have been raised before him in the course of proceedings under Sec. 66 (2), provided they arise out of the order of the Assistant Commissioner or Commissioner in appeal. The assessee is under no duty to formulate questions of law and it is sufficient if he indicates that the order of the Commissioner or the Assistant Commissioner gives rise to questions of law.

Adat charges incurred during the account year but not paid before the close of the year are not expenditure incurred for earning the profits of the account year within the meaning of Sec. 10 (2) (ix) or Sec. 11 (2) of the Act.

Case (Misc. Reference No. 20-B of 1927), stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Central Provinces and Berar, in compliance with an order of the Court.

CASE.

As directed in the above quoted order** of the Hon'ble the Additional Judicial Commissioner, I have the honour to refer the following case for the decision of the Hon'ble the Judges of the said Court under section 66 (3) of the Income-tax Act, XI of 1922.

2. Seth Jainarayan Mhaliram of Shegaon was served with a notice under section 22 (2) on the 12th May 1923 and was asked to make the return of his income for the year ending in Diwali 1922 by the 17th of June 1923. He did not make this return on the due date, but began to apply for extension of time and complained of having lost the notice under section 22 (2). He was twice supplied with the necessary forms and yet he did not make his return till the 22nd November 1923. On the 5th of January 1924, he produced unclosed accounts before the Income-tax Officer. The Assistant Commissioner who, exercising the powers of an Income-tax Officer made assessment in this case, heard the assessee and looked into his accounts. With the exception of the cotton

* (1929) A. I. R. Nag. 243.

** See end of para. 5 *infra*.

accounts of Telhara, they were all "unclosed". The assessee had very extensive business in the purchase and sale of cotton at Telhara and at Shegaon. The closed accounts of Telhara disclosed a total of Rs. 10,00,721 on the credit side and a total of Rs. 9,75,044 on the debit side, thus disclosing a profit of Rs. 25,677. The cotton accounts of Shegaon branch were not closed. There was no opening or closing balance shown there, nor were the transactions taking place shown in weight. They were thus totally unclosed. The sale of cotton amounted to Rs. 16,48,829. The Assistant Commissioner treating them as unclosed deduced the income at 2 per cent. of the total sales. He thus found the income from different sources as:—

	Rs.
Telhara account	.. 25,677
Shegaon account	.. 32,976
Sowda account	.. 51,521
Batta account	.. 1,574
Hundawan account	.. 826
Interest account	.. 2,141
Goduram Mangalchand	.. 777
Cloth account	.. 5,290
Jawala shop	.. 3,356
	<hr/>
Total business income	.. 1,24,138
Income from property	.. 462
	<hr/>
Total income for income-tax	.. 1,24,600
Partnerships taxes Rs. 70,000	.. 35,000
Malkapur partnership	.. 20,305
	<hr/>
Total income for super-tax	.. 1,79,905
	<hr/>

He passed an order on the 20th February 1924, assessing him on an income of Rs. 1,24,600.

3. Being under the impression that as he did not produce his closed accounts he was perhaps assessed under section 23 (4) the assessee put up an application under section 27 on the 13th of March 1924 requesting that the assessment be cancelled and fresh assessment made. This application was rejected on the 31st May 1924 as it was held that the assessment was not under that sub-section. On the 16th June 1924 he appealed under section 30 to the Commissioner and though the appeal was gone time barred it was admitted on the applicant alleging that he was mistaken in understanding the assessment order of the 20th February 1924 and therefore in wasting time in application under section 27, dated the 13th March 1924. The main objection in appeal was that the profits of cotton should not be calculated at 2 per cent. on the sales as in place of this cotton business, business in forward contract was done and profit was made in it. For other objections a list of items under dispute was filed and all these objections are dealt with in my appellate order passed on the 10th September 1924.

4. Not being satisfied with the order so passed, the assessee put in an application dated the 5th October 1924, under section 66 (2), requesting 4 points to be referred to the High Court. As no point of law said to have been involved in this case was expressly mentioned, the applicant was asked to frame the questions of law that arose out of this case and submit them to me. He put in another application which was received in the office on the 20th October 1924. Here too the items under dispute were repeated but no questions of law supposed to have been involved were formulated. Then on the 31st October 1924, his counsel, Mr. Y. R. Dongre, put up another application supposed to be propounding the questions of law involved in this case but again merely referring to the items on which objections had been taken before. It still did not appear to me as to what point of law arose out of this case and on what point of law the reference to the High Court was sought. It was held that no point of law was involved and the reference was refused: *vide* copy of order dated the 31st October 1924.

5. About the 28th of April 1925, the assessee then put up an application in the Court of the Judicial Commissioner requesting the said Court to order the Commissioner of Income-tax to state the case. A copy of this application was sent to me under cover of your letter No. 324—J. dated the 24th June 1925. According to this application the assessee has asked the following points of law to be referred to the High Court:—

(i) The Kanas Rui Gathan Khata shows a loss of Rs. 20,272. It is unreasonable and arbitrary to hold that the applicant's profit ought to be calculated at the rate of 2 per cent. on the amount of sale proceeds in this Khata. This profit figure thus comes to Rs. 16,48,859. The learned Commissioner was shown how the loss of Rs. 20,272 could be ascertained and his reason for rejecting the figure of loss or ignoring the contention that there was loss is illegal.

(ii) The Income-tax Officers erred in law in keeping separate the Clearing House Khata and the Kapas Rui Gathan Khata as the forward sales entered in the Clearing House Khata were made to make certain profits or keep down the loss of the Kapas Rui Gathan Khata.

(iii) The transactions of sales and purchases of the Telhara branch of the applicants were carried on at Telhara in the Adat of the firm of Meghraj Bansidhar of Telhara. The latter deserves to get his adat charges for his services before the Diwali of 1929 and the applicants were bound to credit the adat charges of Rs. 4,692-6-0 in the account of the Adatva Meghraj Bansidhar before the Diwali of 1929. Question is whether the applicants are not entitled in law to have deduction for this amount in settling the figure of assessable income at the Telhara branch as per section 11 (2) of the Income-tax Act, irrespective of the fact that the actual payment of the adat charges came to be made to the Adatva when the whole account was settled later on.

(iv) That under section 11 (2) and the general principles of ascertaining taxable income the petitioners are entitled to get deduction of Rs. 4,468-13-0 from the profits of the Chillar Khata, as the amount had to be paid as interest to others for the business.

(v) That under section 11 (2) the petitioners are entitled to get similar deduction on account of interest paid to others and of the salaries of servants in computing the profits on the gross sales of cloth.

On the 16th February 1927, the Hon'ble the Additional Judicial Commissioner passed the following order:—

“Having considered the questions formulated for reference and the arguments advanced on both sides I am of opinion that the Commissioner's decision that no questions of law are involved is not correct. I therefore acting under the powers vested on me by the provisions of section 66 (3) of the Indian Income-tax Act require the Commissioner to state the case and refer it to this Court. I make no order as to costs.”

6. There were three sets of so-called questions of law put up before me for reference to the High Court, and a fourth set of them came to be filed before the Hon'ble the Additional Judicial Commissioner. Though all these four sets of questions seem to refer to practically the same items, the wordings of each set of them make them different from other sets and I am rather in a doubt as to which set of questions I am ordered to refer to the Hon'ble Court. If I understand the concise order quoted above in full correctly, it appears to me that the questions as formulated and presented before the Hon'ble the Additional Judicial Commissioner are to be referred to that Court. As regards this I beg to take the preliminary objection that the petitioner is not entitled to have these questions referred to the High Court under section 66 (3). The question is, “Whether or not an assessee is entitled to move the High Court for a direction to the Commissioner to refer questions of law which have not been raised before him in the course of the proceedings under section 66 (2) of the Income-tax Act?” This section says that “Within one month..... an assessee..... may..... require the Commissioner to refer to the High Court any question of law arising out of such order.....” This section requires the assessee to therefore frame the questions which he wants the Commissioner to refer to the High Court and those questions must arise out of the order passed under section 31 or section 32. If his application for reference to the High Court is refused, on the ground that no question of law arises, then it is for the assessee under sub-section (3) of the same section to apply to the High Court within a particular period to require the Commissioner to state the case and refer the same questions of law for the decision of the High Court. It thus follows that the assessee could not ask the High Court for a fresh set of questions of law being referred to it and I would request the decision of the Hon'ble Judges on this point for my future guidance.

7. If it is held that even fresh questions could be referred to the High Court I would then give my opinion on each question raised by the assessee in his application dated the 28th April 1925 as follows.

8. *Question (i).*—It is wrong to say that the Kapas Rui Gathan Khata showed a loss of Rs. 20,272. This account was not made up till after the assessment was made by the Assistant Commissioner. It was left unclosed. The account was made up after the order was passed by the Assistant Commissioner who made the assessment in this case. Even then it was looked into for what it was worth. The weights of the bales were even then not given, nor was the closing stock of Rui or Sarkhi, i.e., oil-seeds shown. In fact it was stated that nothing was left at the end of the year, though at the beginning of it, the opening stock was valued at Rs. 91,982-1-0. Until the actual weight of the cotton in hand in the beginning of the year, of the cotton purchased during the year, of the cotton sold during the year and of the cotton remaining at the end of the year were given, it was impossible to call these accounts as complete

and reliable. In fine, these accounts could not be called what is technically known as "Closed accounts". The assessing officer was therefore justified from the state of the accounts to call them "unclosed", that is to say, accounts of which the opening and closing stock and the purchase and selling quantities were not ascertainable. In all "unclosed" accounts a certain percentage rate or what is called "a fair margin of profit" is applied for the purposes of calculating the profits. It is wrong to say that it was unreasonable and arbitrary to hold that the applicant's profits should be calculated at 2 per cent. on the sale proceeds in this Khata. In this particular season and in this very assessee's shop at Telhara, not far from Shegaon, where he had maintained accounts in "closed" form, on a total transaction of Rs. 10,00,721 the profits found were Rs. 25,677. That came to over 2.5 per cent. of the total sales and this was the fair average rate at which the profit on the total sales of Rs. 16,48,829 should have been calculated by the Assistant Commissioner in the Shegaon shop also. He was lenient and calculated the profits at 2 per cent only. In the face of these facts of the case, it appears wonderful for the assessee to allege that it was unreasonable and arbitrary to calculate profits at 2 per cent. It is wrongly asserted that the profit figure comes to Rs. 16,48,829. This is the sale figure. The total sales of Shegaon cotton shop came to Rs. 16,48,829 and profits at 2 per cent came only to Rs. 32,976. The Commissioner could not believe in the imaginary loss of Rs. 20,272 in this cotton shop. This loss was not proved nor could it be, as the weights of cotton were not given. The accounts were not complete for reasons given before. There is no illegality in treating the accounts for what they were.

9. Question (ii).—I fail to understand how this question arises out of the order passed in appeal under section 31. Neither in the grounds of appeal nor in the appellate order is it said that the Clearing House Khata and the Kapas Rui Gathan Khata were kept as one; nor, as a matter of fact, were they kept as one. It might have been the intention of the assessee to set up the loss of one Khata against the profits of another and this would, under the ordinary rules of computing income for income-tax purposes, have been allowed *ipso facto*, but by putting a question of this kind a wrong impression seems meant to be created that the loss of one Khata was not taken into account against the profits of another. In the Bombay Clearing Account (Speculation) or the Souda Khata as it is called, the credit side was Rs. 1,43,164, and the debit side Rs. 91,643. Thus the profit was Rs. 51,521. If there was a loss in the Rui Gathan Khata which was a separate account and which dealt with the purchase of cotton at Shegaon, it would surely have been debited against this; but as shown above, there was no loss in the Kapas Khata and none could be set off against the Souda Khata.

10. Question (iii).—It is only as regards this point that the question now seems to have been correctly worded as given in its latter part. The fact is that the payment of Rs. 4,692-6-0 was actually made to Seth Meghraj Bansidhar seen, had closed. As the actual payment did not come to be made in the account year its set off could not be allowed. Unless the money is actually spent in the year, it cannot be said to be a payment in it and as such deduction on that account cannot be granted.

11. Question (iv).—This question of law, if it be so called, is beside the point. It ought to have been said as to how this amount of Rs. 4,468-13-0 was spent for purposes of profession or vocation to be allowed under section 11 (2). No details of it are given here and from the order passed in appeal it is apparent

that the item of Rs. 1,748-15-3 paid to Shriram Shaligram of Shegaon was not allowed because entry regarding it was made after the assessment order was passed and after the accounts were inspected. It was held to be of a doubtful nature and was disallowed on that account.

12. *Question (v).*—It is difficult to understand as to how this question arises out of the facts of the case. In the appellate order dated the 10th September 1924, there is no mention of “interest paid to others” regarding which this question is raised. As regards the salary of servants, para 7 of the appellate order says that the whole of the amount for which objection was taken by the assessee was allowed. Therefore it is unnecessary to reply this question.

13. I think for reasons given above the application should fail.

A. V. Khare, for the assessee.

D. N. Choudhary, for the Crown.

JUDGMENT.

KINKHEDE, A. J. C.:—This is a case referred for decision to this Court by the Commissioner of Income-tax under section 66 (3) of the Indian Income-tax Act (XI of 1922), upon a requisition made by this Court as per its order dated 16—2—1927. The facts are stated in sufficient details by the Commissioner of Income-tax in his reference and I need not repeat them here.

2. The assessee had filed a return showing Rs. 20,374-9-6 as his approximate (Ajmasa) income for the year ending Diwali 1922. He could not vouchsafe for the correctness of his figures as required by law, as is clear from the word ‘Ajmasa’ (approximately) used by him. This was not accepted, as the Assistant Commissioner himself puts it, “as he was said to have a large trade in cotton. The Assistant Commissioner asked him to produce his account books which being produced were inspected and found to be ‘unclosed.’” He was asked to close them, but he pleaded his inability to close them for want of accounts from other firms with which he had dealings.

3. After some investigation the Assistant Commissioner assessed him on a total income of Rs. 1,79,900 and by an order dated 20-2-1924, directed him to pay Rs. 17,453-10-0 on account of income-tax and super-tax. The assessee appealed to the Commissioner who ordered reduction of the tax by Rs. 2,884-5-0. Not being satisfied, he applied to the Commissioner of Income-tax to state his case on points formulated by him but the Commissioner thinking that they did not constitute points of law, asked him to submit a revised petition. But even then the Commissioner was not satisfied, and the assessee then put in a 3rd application through a pleader. Still it was not clear “as to what point of law arose out of this case and on what point of law the reference to the High Court was sought.” The application was, therefore, refused.

4. The assessee then presented a petition to this Court setting forth the points of law arising out of the Commissioner’s order. Both parties were heard, and this Court passed the order dated 16—2—1927, compelling the Commissioner to make the reference. The Commissioner in submitting the case as ordered has raised a preliminary question and requested this Court to decide it before giving its opinion on the points raised. That question is whether or not an assessee is entitled to move the High Court for a direction to the

Commissioner to refer questions of law which have not been raised before him in the course of the proceedings under section 66 (2) of the Income-tax Act?

5. Before dealing with the questions referred, it is necessary to dispose of this preliminary objection. In my opinion, the wording of section 66 (2) does not bear the construction put by the Commissioner. It does not lay on the assessee the duty of formulating any questions of law, although it is open to him to do so for the benefit of the Commissioner. It ought to be sufficient for him to indicate that the order of the Commissioner upholding the assessment gives rise to questions of law and that he wants him to state his case for the decision of this Court. The law casts on the Commissioner the duty of drawing up a statement of the case. Had the wording of the section been that the petition for reference shall be drawn up in the form laid down for a memo. of appeal under section 30 (3) or 32 (2) of the Income-tax Act and shall also specify the questions of law, then there was some force in the contention raised by the Commissioner. No rules or departmental instructions have been brought to my notice by the learned counsel who appeared for the Commissioner, making it obligatory on the assessee to specify or even to formulate the questions of law arising out of the Commissioner's order at the time when he moves the Commissioner to state his case under section 66 of the Act. It thus follows that the duty of stating the case for the decision of the High Court in such a clear manner as "to enable it to determine the question raised thereby" rests on the Commissioner and not on the assessee. After the Commissioner refused to state his case, the law vests in the assessee the right to move this Court for compelling the Commissioner to make a reference on the ground that his case involves questions of law, and this Court on being satisfied that the Commissioner's view that no questions of law are involved is not correct, can issue directions to him to state the case. It is sufficient for the purposes of the reference if the questions set forth in the petition to this Court arise out of the Commissioner's order passed under section 31 or section 32 of the Act. I, therefore, hold that an assessee is entitled to move the High Court for a direction to the Commissioner to refer questions of law raised by him in his petition to this Court even though they may not have been raised before him in the course of the proceedings under section 66 (2) of Income-tax Act, provided that they are questions of law arising out of the Commissioner's order passed in appeal. For these reasons I overrule the preliminary objection and proceed to deal with the questions involved in the reference.

6. The Assistant Commissioner stated in his order of assessment that the accounts of the Shegaon business which were examined and scrutinized by the Income-tax Officer as also by himself disclosed that they were "unclosed accounts" and that the total turn-over was of Rs. 16,48,928. The Income-tax Officer, therefore, applied $2\frac{1}{2}$ per cent rate, whereas the Assistant Commissioner reduced it to 2 per cent. The Commissioner has upheld this rate. He says it is not an unreasonable or arbitrary rate.

7. The scheme of the Income-tax Act shows that under section 22 and section 23 (4) it is the duty of the assessee to supply the materials of his assessment. If he fails to supply or having supplied fails to substantiate the same under section 23 (3) the Income-tax Officer has still "to assess the total income of the assessee" "to the best of his judgment" as contemplated by section 23 (4). The assessee's accounts being unclosed he was unable to supply the full material, much less to substantiate the same. Realizing this difficulty the assessee's agent in his oral statement dated 11-1-1924, before the Income-tax Officer expressly admitted that he had nothing to say if some fair percentage

is adopted to find out his income from the cotton business of Shegaon. The owner of the shop also did not object to the adoption of a percentage. He simply objected to the rate of $2\frac{1}{2}$ per cent. as being high. On the facts ascertained by the Assistant Commissioner in his enquiry he had no reason to think that the rate of 2 per cent. was unreasonable and the Commissioner also had confirmed the same. The reasonableness or otherwise of the rate applied cannot be a question of law which he can agitate before us. Had the assessee disputed in his statement the authority of the Income-tax Department to adopt a flat rate, then I think a question of law might have arisen for consideration "as to whether in the absence of other reliable data as to income of an assessee from a certain source an Income-tax Officer is justified in making an assessment based on a formula deduced by taking a certain percentage of the gross turn-over, as representing a fair margin of profit." But on the admission made by the assessee in this behalf that question does not arise. Therefore it follows that it is not open to him to argue merely the question of the unreasonableness of the extent of the percentage adopted.

8. I am satisfied that the opinion given by the Commissioner on the 2nd point leaves no ground for complaint. I, therefore, held that it does not raise any question of law.

9. I now come to the 3rd point. It raises a question of law whether the assessee is not entitled in law to deduct the Adat charges Rs. 4,692-6-0 payable but not paid to the Adatya from the amount of the gross income derived from the business of purchases and sales of the Telahara branch carried on by him in the Adat of another firm, irrespective of the fact that the actual payment of the Adat charges came to be made to the Adtya when the whole account was settled later on. It is an admitted fact that even though the liability for adat charges was incurred during the Sambat year 1978-79, the same had not been paid to the Adatya before the close of the year. The Commissioner, was therefore, right in disallowing this item as it was not "*expenditure incurred*" for earning the profits of the account year within the meaning of section 10 (ix), or section 11 (2) of the said Act. No doubt it could be termed a *liability incurred* so long it is not satisfied. But it appears the Income-tax Act for obvious reasons does not take into account mere monetary obligations or liabilities incurred. The Income-tax Commissioner was, therefore, right in refusing to allow this deduction.

10. The sum of Rs. 4,468-13-0 paid on account of interest to others for the business would certainly be debitable against the gross income of the business under section 11 (2) of the Income-tax Act. The Commissioner's opinion shows that he might have allowed these deductions had the assessee furnished the necessary details and shown that the payment made was before the end of the account year. A part of this amount was paid after the assessment order was made, i.e., after the accounts were examined. Thus the Commissioner entertained doubts about the correctness of the debit and thought fit to disallow it. My answer to this question is that an assessee is not entitled to deduct any expenditure not actually incurred by him before the close of the account year and that a deduction can be claimed only if the expenditure is actually *incurred* or the liability incurred is satisfied before the close of the year.

HALLIFAX, A. J. C.:—I agree with my learned brother in the general conclusion of his judgment delivered two days before my return from three months' leave. The petitioner has put in from time to time four lists of verbose

and involved arguments or contentions. To understand them involves considerable labour, but they all seem to cover the same ground. My learned brother was "of opinion that the Commissioner's decision that no questions of law are involved is not correct" and required the Commissioner "to state the case and refer it to this Court." The point of law which he was to refer, with his statement of the case on it, was not mentioned.

(2) It may be correct to say that the petitioner may raise questions in this Court which he never raised before the Commissioner, though it would certainly be difficult to do so, but that hardly needs consideration as no question, whether of law or of fact, was raised in this Court that had not already been raised three times before the Commissioner. But I am at a loss to see how the Commissioner can refer a question of law to the Court, with a statement of the case on it, unless it is formulated for him. The Commissioner was apparently aware of this, but he has courteously done his best by stating the case on all the points raised in the petition presented to this Court, whether of fact or law.

(3) But after a laborious examination of all the petitions I am still unable to discover a single question of law in any one of them. The only questions that emerge from them are these:—

1. Was the income derived from the Shegaon business less than 2 per cent. of the total "turn-over"?
2. Is money that a person owes, but has not paid and may never pay, money that he has expended?
3. Can a sum of Rs. 4,692-8-0 admittedly not expended during the year in question be called money expended in that year?
4. Was a sum of Rs. 4,468-13-0 spent at all "for purposes of profession or vocation" or as interest?

The Commissioner's answer in the negative to each of these questions of pure fact is undoubtedly correct, as my learned brother holds, and indeed it would be hard to answer any one of them incorrectly. But we are not concerned with questions of fact.

(4) I am of opinion further that the assessee should be ordered to pay the whole of the costs of these proceedings, including a pleader's fee of fifty rupees.

All the costs of these proceedings will be paid by the assessee, and will include a pleader's fee of fifty rupees.

(260) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Mr. Justice Devadoss and Mr. Justice Mackay.

(31st July 1928).

Raja Rajeswara Sethupathi, Rajah of Ramnad .. Appellant.*

vs.

The Secretary of State for India in Council .. Respondent.

Income-tax Act (VII of 1918), Sec. 52—Assessment on income outside the Act—Bar of suit, scope of—Income from permanently settled estates—If exempt

* (1929) I.L.R. 52 Mad. 12 ; 55 M.L.J. 770 ; 28 L.W. 667 ; A.I.R. (1929) Mad. 179.

from assessment—Mistaken inclusion in return of non-taxable income—Tax paid thereon—Suit for recovery, if lies.

An assessment on agricultural income or income not earned in or brought into British India would be beyond the scope of the Income-tax Act and hence a suit to recover income-tax assessed thereon is not barred by Sec. 52 of the Income-tax Act (VII of 1918).

Income derived from permanently settled estates is outside of the scope of the Income-tax Act by reason of the Permanent Settlement Regulation and the sannads issued thereunder.

Where an assessee mistakenly included in his income-tax return income not taxable under the Act and on an assessment based on the return paid income-tax thereon,

HELD, that the payment being a voluntary one made under a mistake as to the general law of British India and not under duress or coercion, no suit would lie for recovery of the tax so paid.

Appeal [A. S. 95 of 1927] against the decree of the Court of the Subordinate Judge of Ramnad at Madura, dated 29th November, 1926, in O. S. No. 38 of 1925.

A. Krishnaswami Iyer, for the Appellant.

The Government Pleader, for the Respondent.

JUDGMENT.

This appeal is by the Rajah of Ramnad against the decree of the Additional Subordinate Judge of Ramnad at Madura dismissing his suit for the recovery of certain amounts paid by him as income-tax for three years. The Rajah of Ramnad was asked by the Income-tax Officer to make a return of his income taxable under the Income-tax Act (VII of 1918) under section 17 (2) read with section 2, clause (13). He submitted a return for the years 1919-1920, 1920-1921, and 1921-1922, in which he showed the income derived by him from forests and fisheries. The Income-tax Officer, on the basis of the return, proceeded to assess the income from forests and fisheries under section 18 of the Act. The Rajah paid the tax on 5th July, 1920, 25th April, 1921, and 21st April, 1922. He brought the suit on 22nd June 1925, for the recovery of the three sums paid on the dates abovementioned on the ground that the income from forests and fisheries derived from his permanently settled zamindari was not taxable under the Income-tax Act.

The first point urged by Mr. Krishnaswami Iyer for the appellant is that the income derived from a permanently settled estate is outside the scope of the Income-tax Act by reason of the Permanent Settlement Regulation XXV of 1802 and the sanad issued under the Act, and the act of the Income-tax Officer being *ultra vires* he is entitled to a refund of the amount paid by him. In the view we take of the next point, it is unnecessary to discuss all the authorities bearing on this point in detail. In *The Chief Commissioner of Income-tax v. Zamindar of Singampatti*,⁽¹⁾ a Full Bench of this Court held that, where the peishcush of a permanently settled estate was fixed in commutation, not only of the rentals of the cultivated lands but also of all income which might be derived from forests

(1) 1 I.T.C 181.

or fisheries, both under the terms of the sanad and of section 1 of Regulation XXV of 1802, these incomes were exempt from further taxation by the Government, and section 3 of the Income-tax Act did not abrogate this exemption. The learned Judges considered the effect of the Permanent Settlement Regulation of 1802 and the terms of the grant to which the grant in the present case is similar and came to the conclusion that the income derived from forests and fisheries in the permanently settled estate was not liable to be taxed under the Income-tax Act. The learned Government Pleader attacks the correctness of this decision and contends that income from forests and fisheries is taxable unless it comes within the exceptions provided in the Income-tax Act. He urges that there must be specific legislation exempting such income and that it cannot be exempted by implication. Sitting as a Division Bench, we are bound by the decision of the Full Bench. We may observe that we entirely concur with the reasoning and conclusion of the learned Judges who were members of the Full Bench. Reliance is placed by the learned Government Pleader on *Emperor v. Probhat Chandra Barua*(1), *Emperor v. Indu Bhusan Sarkar*(2), *Emperor v. Probhat Chandra Barua*(3), and *Maharajathiraj of Dharbhanga v. The Commissioner of Income-tax*(4), as supporting his contention that the *Chief Commissioner of Income-tax v. Zamindar of Singampatti*(5), was not correctly decided. In *Emperor v. Probhat Chandra Barua*(1), there was a difference of opinion between Rankin, J. and Page, J., Page, J., approving of the decision in *The Chief Commissioner of Income-tax v. Zamindar of Singampatti*(5). In *Emperor v. Indu Bhusan Sarkar*(2), *The Chief Commissioner of Income-tax v. Zamindar of Singampatti*(1) and *Maharajadhiraj of Dharbhanga v. The Commissioner of Income-tax*(4), were followed by a Bench of the Calcutta High Court. In *Emperor v. Probhat Chandra Barua*(3), there was a difference of opinion, two judges approving the Madras view and three judges following the view of Rankin, J., in *Emperor v. Probhat Chandra Barua*(4). In *Maharajadhiraj of Dharbhanga v. The Commissioner of Income-tax*(4), Dawson Miller, C. J., after an exhaustive examination of the Permanent Settlement Regulation and its effect observed: "I see no reason to take a different view from that held by the Madras High Court", while Mullick, J., took a different view. We find this point in favour of the appellant.

It is contended by the learned Government Pleader that no civil suit would lie to recover an amount paid as income-tax. A civil suit is barred under section 52 of the Income-tax Act of 1918. If the tax was levied under the Act, no doubt a suit would be barred, but if the assessment was made in respect of an item of income which is not assessable under the Act, a civil suit would lie to recover it, inasmuch as the Officer making the assessment had no jurisdiction to make it. In cases in which the Income-tax Officer has to decide whether a certain item of income is assessable or not, his decision cannot be said to be *ultra vires* even if it is illegal. But where a certain income is outside the scope of the Act, such as agricultural income or income not earned in or brought into British India, any assessment in respect of such income would be beyond the scope of the Act and a civil suit to recover it would not be barred by reason of section 52. We do not discuss this point at length as we find the next point against the appellant.

The next point is whether the appellant is entitled to recover the money paid under a mistake of law. As already observed three payments were made on 5th July, 1920, 25th April 1921 and 21st April 1922, and the suit was brought

(1) 1 I. T. C. 234.

(2) 2 I. T. C. 221.

(3) 2 I. T. C. 392.

(4) 1 I. T. C. 410.

(5) 1 I. T. C. 181.

on 22nd June 1925. The suit in respect of the first two payments is clearly barred as it was brought more than three years after the date of payment. As the Court of institution closed on 20th April 1925, and re-opened on 22nd June 1925, the last payment was within the period of limitation. Granting that section 14 does not apply to the case, the question is whether the amount paid on 21st April 1922, could be recovered in the circumstances of the case. It is well established that a payment made under a mistake of law cannot be recovered, but it is urged for the appellant that the payment was made under duress or coercion and therefore the amount is recoverable. The decision in *The Chief Commissioner of Income-tax v. Zamindar of Singampatti*(1), was on 21st February, 1922. The assessment notice was dated 31st March 1922, and payment was made on 21st April, 1922. The Rajah of Ramnad in his return of taxable income made in pursuance of the Income-tax Act included wrongly the items of income derived from forests and fisheries.

He says this return was made owing to a mistake, and, on the figures submitted by the Rajah of Ramnad, the Income-tax Officer assessed the income under the Income-tax Act. The question is whether the payment was made under duress in order to take it out of the principle that payments under mistake of law cannot be recovered. It is contended for the appellant that the sending of notice by the taxing authority and his assessment amount to duress or coercion in law. The Rajah of his own accord, and, it may be, owing to ignorance of law, included in the items shown as taxable under the Income-tax Act, the income from fisheries and forests and the Income-tax Officer on the basis of that return made the assessment under the Act. There is no evidence that the Income-tax Officer required the appellant to make a return of the income from forests and fisheries. The appellant like all other assesseees was required to make a return of his income for purposes of Income-tax Act and if he chose to include in the return an item of income which was not assessable under the Act and if on the basis of that return the Income-tax Officer assessed the income, and on notice being given, the assessee paid the tax, it cannot be said that it was paid under duress. In *William Whiteley, Ltd. v. The King*(2) the facts were: William Whiteley, Ltd, carried on a large business in which they employed a large number of assistants who had all their meals on the premises and for the service of those meals they employed a large number of men as cooks and waiters, and on the suggestion of the Inland Revenue authorities that the waiters were "male servants" in respect of whom duties were payable, paid for a number of years the duties in respect of such waiters. From 1903, they paid the duties with a protest that the waiters were not "male servants" within the meaning of the Act. In 1906, they refused to pay and upon proceedings being taken for penalties, the Divisional Court held that the waiters were not "male servants" and that the duties were not payable. They then preferred a petition of right to recover back the moneys so paid. Walton, J., held that the moneys having been paid under a mistake, not of fact, but of law, could not be recovered back either on the ground that they were paid under duress or compulsion or on the ground that they were paid in discharge of a demand illegality made under colour of an office. At page 745 he observed:—"The suppliants knew all the facts. They had present to their minds plainly, when these payments were made, that there was a question as to whether upon such servants as those in question, duty was payable. They themselves raised that question and they paid the duties. They could have resisted payment. They must have known that if proceedings were taken for penalties, it would be open to them in such proceedings to raise the question as to whether the duties were payable or not."

(1) 1 I. T. C. 181.

(2) 101 L. T. 741

as they did in fact in 1906..... I think the most that took place was this, that the Officer of Inland Revenue told the suppliants that in his opinion and in the opinion of the Commissioners of Inland Revenue the duties were payable."

With regard to the cases of duress, the learned Judge observes after referring to certain passages in Leake on Contracts:—"In all those cases, in order to have that done which the person making the payment was entitled to have done without a payment, he had to make the payment and some one, who was bound to do something which the person paying the money desired to have done, refused to do his duty unless he was paid the money. If in those circumstances money was paid, then it can be recovered back. There is an element of duress."

The appellant made the return thinking that he was liable. Whatever might have been the state of the law before 21st February 1922, after the decision in *Chief Commissioner of Income-tax v. Zaminder of Singampatti*(1), it could not be said that there was any doubt as to the non-liability of income from forests and fisheries arising out of permanently settled estates. The notice of assessment was on 31st March 1922. The appellant could have preferred an objection to the assessment on the strength of *The Chief Commissioner of Income-tax v. Zamindar of Singampatti*(1), and could have refused to pay the amount even if he was unsuccessful in his representation to the Income-tax authorities that the income from forests and fisheries was not liable to be assessed under the Income-tax Act, and he chose to do none of these things but paid the amount on 21st April 1922, i.e., two months after the decision in *The Chief Commissioner of Income-tax, v. Zamindar of Singampatti*(1). In *Slater v. Mayor, etc., of Burnley*(2), the facts were:—A water rate of £8-15-4 for one quarter's rate in respect of certain houses was demanded by the defendants, the sanitary authority, and paid by the plaintiff, such sum being 5 per cent. on the gross rental of the houses. After this payment, the defendants altered their basis of assessment from gross rental to rateable value as the proper basis of assessment, they being entitled to charge 5 per cent. on the annual value. If the rate had been calculated on the rateable value it would have been £7-3-10. The plaintiff brought an action in a County Court to recover the overcharge of £1-11-6, the difference between the two sums, as being money paid under compulsion. There was no power to distrain for these rates (except when they did not exceed £1 a quarter which did not apply to the present case), but the defendants had the power to cut off the water supply on non-payment of the rate. The County Court Judges held the payment to be a compulsory one, as the defendants had the power to cut off water and gave judgment for the plaintiff. Cave and Wills, JJ., held that the payment was a voluntary payment and could not be recovered back. Cave, J., observed at page 639:—"There is no case which lays it down that a payment under these circumstances is a compulsory payment. If it were so the consequences would be very far reaching. If that were so, no payment of rent to a landlord would be a voluntary payment." Wills, J., observed:—"It seems to me, in these circumstances, that it is idle to say that there is anything like duress, there was nothing in the nature of a threat used: it is simply the ordinary case of a person raising a contention when a demand is made upon him. That is not sufficient to constitute duress so as to prevent a payment being a voluntary one".

The case would be different if for the purpose of getting an official act done a person pays something more than what is proper; for in order to get the

(1) 1 I. T. C. 181.

(2) 59 L. T. 686.

act done he must pay the amount demanded, otherwise, the act would not be done. In such cases it can be said that the payment is not a voluntary payment, nor is it a payment made under a mistake of law. The case in *Hooper v. Mayor and Corporation of Exeter*(1), and the case in *Steele v. Williams* (2), are cases where, in order to get a certain thing done, the plaintiff had to pay the amount demanded. In *Hooper v. Mayor, etc., and Corporation of Exeter*(1), the Corporation of Exeter exacted harbour dues from the plaintiff in respect of exempted articles. The plaintiff paid in ignorance of the exemption. It was held that the plaintiff was entitled to recover back the money so paid. Lord Coleridge, C. J., observed at page 458:—"From the case cited in the course of the argument it is shown that the principle has been laid down that where one exacts money from another and it turns out that, although acquiesced in for years, such exaction is illegal, the money may be recovered as money had and received since such payment could not be considered as voluntary so as to preclude its recovery." The plaintiff in this case could not have landed his limestone, the article exempted, without paying harbour dues.

In *Steele v. Williams*(2), the facts were that the plaintiff's clerk applied to the defendant, a parish clerk, for liberty to search the register book of burials and baptisms. He told the defendant that he did not want certificates, but only to make extracts. The defendant said the charge would be the same whether he made extracts or had certificates. The clerk searched through four years and made 25 extracts, for which the defendant charged him 3s. 6d. each and he accordingly paid the defendant, £4-7-6. It was held first that the charge for extracts was illegal since 6 and 7 Will. IV-c. 86 S. 35 only authorises a charge for a search and for a certified copy and secondly that the payment was not voluntary so as to preclude the plaintiff from recovering back the excess. Park B. observed:—"In the first place I think that there is evidence that this payment was not voluntary but necessary for the exercise of a legal right, and further, I by no means pledge myself to say that the defendant would not have been guilty of extortion in insisting upon it, even without that species of duress, viz., the refusal to allow the party to exercise his legal right, but *colore officii*". Martin, B., observed:—"It is the duty of a person to whom an Act of Parliament gives fees, to receive what is allowed and nothing more. This is more like the case of money paid without consideration—to call it a voluntary payment is an abuse of language."

In both these cases the plaintiff could not have got what he wanted without the payment, and therefore his payment could not be said to be voluntary, but a payment under duress. This point was the subject of decision by a Bench of this Court in a recent case. *Ramesam and Jackson, J. J.*, held in C. R. P. No. 353 of 1926, as follows:—"The Indian Law seems to be clear, namely, that a mistake, in the sense that it is a pure mistake as to law in India, resulting in the payment by one person to another and making it inequitable that the payee should retain the money is no ground for relief." They refer to an observation of Lord Sumner in *Sinclair v. Brugham*(3). The learned Lord observes:—"There is now no ground left for suggesting as a recognizable 'equity' the right to recover money *in personam* merely because it would be the right and fair thing that it should be refunded to the payer."

We hold that the amount paid on 21st April 1922, which is not barred under the three years' rule was made under a mistake of law and of the general

(1) 56 L. J. Q. B. (N. S.) 457.
(2) 8. Ex. 625; 155 E. R. 1502.

(3) (1914) A. C. 398 at p. 456.

law of British India, applicable to all persons in appellant's position holding permanently settled estates, and therefore cannot be recovered. In the result the appeal fails and is dismissed with costs.

The respondent has preferred a memorandum of objections against the order of the Subordinate Judge disallowing his costs. Having regard to all the circumstances in which these payments were made we think that the plaintiff was rightly held not liable for the costs of the suit. The memorandum of objections is also dismissed.

(261) IN THE COURT OF THE JUDICIAL COMMISSIONER, NAGPUR.

*Before Mr. Findlay, Judicial Commissioner and Mr. Prideaux,
Additional Judicial Commissioner.*

(18th August, 1928).

Rao Bahadur D. Laxminarayan

.. Assessee.

v.

The Commissioner of Income-tax, Central Provinces .. Referring Officer.
and Berar.

Income-tax Act (XI of 1922), Sec. 10 (2) (vii) and (ix)—Obsolescence allowance in respect of buildings—Tile factory taken over by Government on payment of compensation—Value of buildings less compensation and depreciation allowances, if a business loss—Res judicata—Applicability to income-tax proceedings.

Under Sec. 10 (2) (vii) of the Income-tax Act, no obsolescence allowance can be claimed in respect of buildings.

The principle of res judicata as applied in Civil Courts does not apply proprio vigore to the decisions of Income-tax authorities.

Under a contract with the Government for the supply of tiles, the buildings forming the tile factory erected by the assessee were taken over by the Government on the expiry of the contract period on payment of Rs. 10,000 as compensation. The assessee claimed the value of the buildings less the compensation amount and the past depreciation allowances as a business loss or expenditure to be allowed in the computation of his assessable income.

HELD, that the loss claimed was a capital loss or expenditure not allowable under section 10 (2) (ix) of the Act.

Case [Misc. Judicial Case No. 36 of 1927] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Central Provinces and Berar, for the opinion of the Court.

CASE.

Rao Bahadur D. Laxminarayan of Kamptee has some mining business. He was also manufacturing tiles and supplying them to the Government under a special contract. He had put up his own building on the land supplied by Government. The contract with the Government expired in 1924. The Government paid Rs. 10,000 as compensation for the building which after the expiry of the contract became Government property.

2. According to the accounts maintained by the Rao Bahadur, the cost of the tile factory buildings after allowing depreciation stood at Rs. 61,997-3-9 in the account year 1924-25 and he claimed that abatement to this extent should be allowed in the assessment of 1925-26. This, however, was disallowed on the ground that it was not written off in that account year as the correspondence between the Rao Bahadur and the Government had not closed, nor was the amount of compensation then to be paid by Government finally settled. In appeal the Commissioner observed as follows:—"Thus the Assistant Commissioner was correct in not allowing this amount as a set off against the income of the year. Any amount that is adjusted reasonably on this account would be allowed a set off when the correspondence on the subject with the Local Government is closed and it is definitely known how much is to be written off and when it is definitely written off in the books of accounts also."

3. In the following account year the question of compensation for the tile factory buildings was settled between the Rao Bahadur and the Government and, as stated above, Rs. 10,000 were paid. Hence in his return of income for assessment in 1926-27 the Rao Bahadur, after taking into consideration the depreciation allowed in the past and the amount of compensation received from the Government, claimed a deduction of Rs. 48,553-3-9 as loss on "The Tile Factory Buildings." This loss has been disallowed by the Income-tax Officer and also by the Assistant Commissioner in appeal on the ground that it is a loss of capital and that the assessee's claim to an allowance under section 10 (2) (vii) on account of obsolescence is inadmissible.

4. The assessee has put in an application asking that the following four points may be referred for the decision of the Hon'ble Judges of the High Court:—

- (a) Whether the Additional Income-tax Officer was justified in holding that the buildings, constituting plants, moulds, etc., for the manufacture of tiles, did not fall in the category of the word 'plant' as used in section 10 (2) (vii) of the Act and the claim for deduction was not permissible thereunder?
- (b) Whether the Additional Income-tax Officer was right in holding that the essential condition for allowing obsolescence allowance was replacement alone and whether his finding would cover cases in which the possession of the property had perforce to be relinquished?
- (c) Whether in view of the clear orders of the Commissioner of Income-tax, the final authority on questions of fact, to grant the set off in respect of the same item, the Income-tax Officer or the Assistant Commissioner has jurisdiction to ignore the said decision and to go behind his superiors' orders contained in a judicial proceeding on the same subject and to give an adverse finding?
- (d) Whether, under the circumstances of the case, the claim for the deduction of the loss incurred by the assessee in the taking over of the buildings, etc., by the Government, was not a business loss to be allowed in the computation of the income of the petitioner assessable under the Act?

5. I beg to submit my opinion on the above points as follows:—

Question (a):—The question is curiously worded. The expression "buildings constituting plants, moulds, etc." is meaningless. "Buildings" are

not "plant" as applicant himself admitted before the Assistant Commissioner on 23rd September 1925. Neither are moulds in any sense of the word with which I am familiar "buildings." The sum of Rs. 48,553-3-9 represents the cost of buildings not of plant. The applicant has always shown the cost of buildings and the cost of plant separately (as was indeed inevitable) for the purpose of claiming the depreciation allowance. In his application dated the 9th May 1925 he valued the tile factory *buildings* at Rs. 68,885-3-9 after allowing depreciation. After allowing further depreciation and deducting the amount of compensation paid by Government the loss is now put at Rs. 48,553-3-9. It is really immaterial, however, whether the sum in question represents the cost of buildings or of plant because (1) the Act does not allow any deduction on account of 'obsolescence' in respect of buildings and (2) as I shall explain below no question of 'obsolescence' arises in this case at all. I therefore submit that this question should be answered in the affirmative, so far as it is susceptible of being answered at all.

Question (b):—In the first place this question does not arise. For, as observed above, no obsolescence allowance is granted in respect of buildings. Section 10 (2) (vii) is applicable only to machinery or plant and not to buildings. In the second place, the "obsolescence" allowance is given as its name implies in respect of something that has become *obsolete* and therefore has to be got rid of. In the case of *Ratansingh, v. Commissioner of Income-tax, Madras*, (1) the High Court of Madras has held that the word "obsolete" as applied to "machinery means machinery which has gone out of date because it has been superseded by later machinery more suitable to its purpose and therefore although able to perform its functions, it is not in common parlance sufficiently up-to-date to make it machinery that a prudent man would continue to use, but machinery which he would replace as being in the ordinary meaning of the term obsolete." In the present case there is no question of any plant having become obsolete and therefore there can equally be no question of an allowance on account of "obsolescence", I submit therefore that this question also should be answered in the affirmative.

Question (c):—This question proceeds on the assumption that the Commissioner of Income-tax is the final authority on questions of fact, that the question under consideration is a question of fact and that an observation of the Commissioner in regard to the proper manner in which an assessment should be made in the future is legally binding on himself and his subordinates. Such is, however, not the case. This question regarding the obsolescence allowance is a question of law and if it had been a question of fact it could not have been referred to your Lordships. The Commissioner of Income-tax has no power under the Act to issue rulings, whether on question of law or of fact, that will bind either himself or his subordinate officers in future proceedings. No question of estoppel or of *res judicata* can possibly arise. It was the duty of the Assistant Commissioner to follow the law, irrespective of any *dicta* of the Commissioner of Income-tax in regard to a different assessment and the only question for consideration now is whether the Assistant Commissioner's action was in accordance with the law or not. I submit that it was in accordance with the law and that therefore this question should be answered in the affirmative.

Question (d):—The applicant is here apparently putting forward an alternative claim in case the claim to an allowance on account of 'obsolescence' should fail. He claims here that the sum under consideration represents a "business loss." No such term is to be found in section 10 of the Act and only

such deductions from the gross income, profits or gains are admissible as are specified in that section. What the applicant is really claiming is capital expenditure incurred many years ago. Even if the "loss" be regarded as "notional expenditure" of the year in which it occurred it is still capital expenditure, and section 10 (2) (ix) specifically excludes capital expenditure from the category of admissible deductions. Nor in any case, I may remark in passing, is it clear how this notional expenditure could be held to have been incurred for the purpose of earning the profits and gains against which the applicant claims to set it off. It is so obvious however that this is a capital loss, and the principle that capital losses (like accretions to or appreciation of capital, or the sale proceeds of capital assets) cannot be taken into account in computing income for the purpose of assessing income-tax that I do not consider it necessary to elaborate the point.

I submit, therefore, that this question should be answered in the negative.

G. L. Subhedar, for the Assessee.

D. N. Choudhari, for the Crown.

JUDGMENT.

(1) This is a reference made by the Commissioner of Income-tax under section 66 of the Income-tax Act. The non-applicant Rao Bahadur D. Laxminarayan of Kamptee supplied tiles under a special contract to Government for five years which expired in 1924. Thereafter, the building erected on the land supplied by Government passed to the latter under the terms of the agreement, Government paying Rs. 10,000 as compensation to the non-applicant. The non-applicant's case was that a loss of Rs. 48,553-3-9, which he incurred on the Tiles Factory building, should have been allowed for in his income-tax assessment for the year 1926-27. Four questions have been referred for our decision in this case; these are as follows:—

- (a) Whether the Additional Income-tax Officer was justified in holding that the buildings constituting plants, moulds, etc., for the manufacture of tiles did not fall in the category of the word 'plant' as used in section 10 (2) (vii) of the Act and the claim for deduction was not permissible thereunder?
- (b) Whether the Additional Income-tax Officer was right in holding that the essential condition for allowing obsolescence allowance was replacement alone and whether his finding would cover cases in which the possession of the property had perforce to be relinquished?
- (c) Whether in view of the clear orders of the Commissioner of Income-tax, the final authority on questions of fact, to grant the set-off in respect of the same item, the Income-tax Officer or the Asst. Commissioner has jurisdiction to ignore the said decision and to go behind the superior's order contained in judicial proceedings on the same subject and to give an adverse finding?
- d) Whether, under the circumstance of the case, the claim for the deduction of the loss incurred by the assessee in the taking over of the buildings, etc., by the Government, was not a business loss to be allowed in the computation of the income of the petitioner assessable under the Act?

(2) The case is not one which requires any detailed consideration at the hands of this Court, because it is obvious that, on none of the four points attempted to be raised, the non-applicant's contentions have any substance whatever. As regards the first question, we only desire to say that it was framed in an ambiguous and question-begging fashion in so far as the expression "buildings constituting plants, moulds, etc.," is concerned. As is perfectly obvious from section 10, sub-section (2) (iv) and (vii) of the Income-tax Act, a clear distinction is laid down therein between "buildings" as compared with "machinery, plant". We are aware that, under particular statutes in England, plant may also include a building, but we are not concerned here with English law or with any particular English statute and, from the provision just referred to, it is perfectly obvious that a clear distinction is laid down between "buildings" as compared with "machinery" and "plant". Equally obviously no question arises of obsolescence allowance in respect of a building nor indeed, as the Commissioner of Income-tax has pointed out, can in the nature of things, any question arise of obsolescence in connection with particular buildings. We accordingly answer the first question in the affirmative.

(3) The second question does not, in our opinion, therefore, require any answer because, as we have held, no obsolescence allowance can be allowed in respect of buildings, and we do not, therefore, propose dealing with the question of whether the essential condition for allowing obsolescence allowance is replacement alone.

(4) We are also unable to see that the non-applicant has any case as regards the third question. We know of no ground for holding that the principles of *res judicata* as applied in the Civil Courts apply *proprio vigore* to the decisions of the income-tax authorities. The non-applicant's grievance is that, in a previous appeal, the Commissioner of Income-tax had indicated that a question of whether the non-applicant could be granted an obsolescence allowance in connection with buildings would be one for consideration in a subsequent order. We know of no authority for the view that officers subordinate to the Commissioner of Income-tax were necessarily bound by any *dictum* of the Commissioner—a *dictum*, in this instance which apparently proceeded on, or indicated, a wrong view of the Income-tax law applicable. On the contrary it was the duty of the Assistant Commissioner to follow that law and this, in our opinion, he has done. We, therefore, answer the third question in the affirmative.

(5) As regards the fourth question, we are unable to see any ground for finding that the capital loss to the non-applicant as incurred was a business loss or expenditure which he could claim for under the Income-tax Act. The learned counsel for the non-applicant has suggested here that the buildings might be regarded as stock-in-trade, but in our opinion, the loss said to have been incurred by the non-applicant in connection with the buildings was clearly a capital expenditure or loss, and the principle that capital losses cannot be allowed for under section 10 of the Income-tax Act, is distinctly laid down in sub-section (2) (ix) thereof. We therefore, answer the fourth question referred to us in the negative.

(6) We may add that, in the course of argument, it was suggested on behalf of the non-applicant that the loss in question might be brought under clause (vi) of sub-section (2) of section 10. The point is, however, not before us and we do not think that, in the circumstances, we are entitled to consider it. We accordingly answer the fourth question as stated above.

(7) The non-applicant must bear the applicant's costs. We fix Rs. 50 as pleader's fees.

(262) IN THE CHIEF COURT OF OUDH AT LUCKNOW

*Before Sir Louis Stuart, Kt., Chief Justice and
Mr. Justice Bisheshwar Nath Srivastava.*

(27th August, 1928)

Lal Jagmohandas Rastogi

Assessee.*

v.

The Commissioner of Income-tax, United Provinces. . . Referring Officer.

Income-tax Act (XI of 1922) Sec. 4 (3) (vii)—Order of Court staying execution of decree—Payment of interest to decree-holder thereunder—If casual income—Litigation expenses, if deductible.

Interest received by a decree-holder under an order of Court granting stay of execution of the decree on the judgment-debtor furnishing security for a specific amount and paying interest thereon at 6 per cent every six months, is income assessable under Sec. 4 of the Income-tax Act and is not income of a casual and non-recurring nature exempt under Sec. 4 (3) (vii) of the Act. On an assessment of such interest receipts no deduction can be allowed in respect of the expenses of the litigation.

Case [Civil Reference No. 7 of 1928] stated under section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, United Provinces, for the opinion of the Chief Court.

CASE.

Lala Jagmohan Das Rastogi was assessed to income-tax by the Income-tax Officer, Lucknow, on November 15, 1927, on the income received in 1925-26 under section 23 (3), read with section 54 of the Income-tax Act, in the circumstances set out in my order of April 7, 1927, of which a copy is contained in appendix A* and on the income received in 1926-27 under section 23 (3).

2. The assessed income of the two years contained items of interest amounting to Rs. 10,968 and Rs. 5,621, respectively, which are explained in the following passage from the appellate order of the Assistant Commissioner of Income-tax:—

“Lalas Inder Prasad and Jagmohan Das, sons of Kanhaiya Lal, were members of an undivided Hindu family until the year 1915. In this year, that is, on September 23, 1915, Lala Inder Prasad sued for the partition of the joint Hindu family property in the court of the Subordinate Judge, Lucknow. A preliminary decree was passed on January 31, 1916, by the Subordinate Judge. The object of this decree was to specify the property which was to be divided. The decree was based on a compromise in which the property was specified. The compromise was of an indefinite character, and sought to apply to property which might come to light later. This left a large opening for the

* A. I. R. (1929) Oudh. 125.

* Not printed.

continuation of the litigation. The litigation was continued. Further property was discovered from time to time, which led to its continuation. It is unnecessary to follow its weary course. On July 25, 1922, the Subordinate Judge gave a final decree for partition. This decree related both to moveable as well as immoveable property. With regard to the immoveable property, it laid down that the defendants (the appellants) were to get Rs. 93,672-15-3, with future interest, until the entire amount was paid. Against this order the plaintiffs appealed to the Judicial Commissioners, who dismissed the appeal on March 10, 1924. On April 3, 1924, leave to appeal to the Privy Council was applied for, which was granted on September 22, 1924. In May 1927, the Privy Council dismissed the appeal. The decree gave the defendant-appellants the following property:—

- (1) House property worth Rs. 53,136-7-0.
- (2) Other immoveable property, that is, shares in certain villages in Lucknow and Cawnpore districts, of which it is unnecessary to mention the valuation.
- (3) Moveable property worth Rs. 79,606-7-11½, *plus* interest amounting to Rs. 14,066-8-1½, total Rs. 93,672-15-3.

Rs. 79,606 include not only the appellant's share of the bonds carrying interest, but also other moveables, such as ornaments, jewellery and village profits which had been appropriated by the plaintiffs in the suit for partition. It is not necessary to decide whether Rs. 14,066-8-1½, the interest, is liable to be assessed in its entirety, or after deduction of any relevant expenses; nor is it necessary to determine here what the expenses in relation to this amount were. It is enough to say that the inclusion of the valuation of the family ornaments and village profits, etc., does not alter the apparent liability of this amount. But it is not this amount which the Income-tax Officer has assessed, that is, the subject of this appeal, and consequently it is not necessary for me to enter into a discussion of its liability in part or whole. On an application for the execution of the decree, the judgment-debtors applied for the stay of execution until, after the grant of leave to appeal, the Privy Council had decided the appeal. For reasons given in his order, dated November 17, 1924. Mr. Justice DALAL, the Judicial Commissioner ordered the execution to be stayed on condition that the judgment-debtors gave security of immoveable property to the satisfaction of the court below to the value of Rs. 95,000, and, at the same time, that they must pay interest on this amount, namely Rs. 95,000, to make up for the delay to the opposite party, namely the decree-holder appellants in this case in recovering the decretal amount. In passing this order, Mr. Justice DALAL fixed the interest on Rs. 95,000 at 6 per cent. and directed that it should be paid regularly on July 1, and January 1, every year, beginning with July 1, 1925. In default of payment of this interest, the Judicial Commissioner ordered that the order of stay should be discharged, and the opposite party should be at liberty to execute the decree in the way best suited to himself. Rupees 10,968, received by the appellant in the year 1925-26, and Rs. 5,620-4-0 in the year 1926-27, which has been assessed by the Income-tax Officer, is the interest on Rs. 95,000 mentioned above.

3. In making the assessment for two years, the Income-tax Officer dealt with the years separately in the assessment forms, but wrote one order explaining both assessments and issued a combined notice of demand. These documents are in the records, which will be produced before the Chief Court.

4. The assessee appealed against the assessment on the grounds that the above items of interest were for various reasons not assessable, that, if they were assessable, the expenditure on the litigation should be allowed, that the provisions of section 34 were not applicable, and that the assessment of the two years should not have been mixed up, while his advocate also argued that, in any case, the income was of a casual and non-recurring nature. The appeal was rejected by the Assistant Commissioner of Income-tax, an extract copy of whose order is attached in appendix B.*

5. The assessee has now demanded a reference to the Chief Court for the reasons given in his petition, dated February 16, 1928, of which a copy is contained in appendix C.*

6. The following questions of law arise:—

- (i) In the circumstances stated, were the sums of Rs. 10,968 and Rs. 5,621 income, to which the Income-tax Act applies within the meaning of section 4 of the Indian Income-tax Act, 1922?
- (ii) Did the income received in 1925-26, which had escaped assessment to income-tax, come within the scope of section 34 of the said Act?
- (iii) Is the claim tenable that the expenditure on the litigation, between the assessee and his brother, should be allowed, under the provisions of section 12 (3) of the said Act, as expenditure incurred solely for the purpose of earning the items of interest in dispute?
- (iv) Were the proceedings of the Income-tax Officer bad in law, because he wrote one order under section 23 (3) of the said Act explaining the assessment made separately?

7. In the opinion of the Commissioner of Income-tax, the answer to the first and second questions is in the affirmative, and to the third and fourth, in the negative. The Commissioner has not referred to the form of the notice of demand in the fourth question, because no appeal lies under section 30 of the Act against action under section 29, and, as a question of law must arise from an appellate order, no such question arises on this point.

D. K. Seth and Mahabir Prasad Srivastava, for the Assessee.

G. H. Thomas, for the Crown.

JUDGMENT.

This is a reference to the Chief Court from the Commissioner of Income-tax under the provisions of section 66, Act XI of 1922. We are asked to answer the following four questions:—

(i) In the circumstances stated, were the sums of Rs. 10,968 and Rs. 5,621 income, to which the Income-tax Act applies, within the meaning of section 4 of the Indian Income-tax Act, 1922?

(ii) Did the income received in 1925-26, which had escaped assessment to income-tax, come within the scope of section 34 of the said Act?

(iii) Is the claim tenable that the expenditure on the litigation between the assessee and his brother, should be allowed, under the provisions of section

12 (3) of the said Act, as expenditure incurred solely for the purpose of earning the items of interest in dispute?

(iv) Were the proceedings of the Income-tax Officer bad in law, because he wrote one order under section 23 (3) of the said Act explaining the assessments made separately?

The facts are as follows. Jagmohan Das, assessee, was a member of a joint Hindu family with his brother Indar Prasad. Indar Prasad instituted a suit for partition. On the 25th July 1922, the Subordinate Judge granted a decree for partition. One condition of this decree was that Jagmohan Das was to receive certain property. Indar Prasad considered that the decree gave Jagmohan Das more than he was entitled to and he appealed to the Court of the Judicial Commissioner. The Judicial Commissioner's Court dismissed his appeal on the 10th March, 1924. Indar Prasad was not satisfied. He applied for leave to appeal to their Lordships of the Judicial Committee. That leave was granted to him. The fact that the leave was granted to him did not prevent Jagmohan Das from executing the decree and Jagmohan Das proceeded to execute the decree. Indar Prasad applied for stay of execution. On the 17th November 1924 Mr. Dalal, the Judicial Commissioner, ordered the execution to be stayed on conditions that Indar Prasad gave security for Rs. 95,000 and further paid interest at 6 per cent. per annum on Rs. 95,000 at certain intervals into the Court. The interest was so paid. It was received by Jagmohan Das. As their Lordships of the Judicial Committee dismissed the appeal there has been no question of recovering it from Jagmohan Das. We are asked in the first place as to whether this interest is "income" to which the Income-tax Act applies. We have no doubt as to the fact that it is "income" to which the Income-tax Act applies within the meaning of section 4. The position was this. If Indar Prasad had at once complied with the terms of the decree Jagmohan Das would have obtained this property. From this property he could have obtained an income. Owing to Indar Prasad taking the case to their Lordships of the Judicial Committee the enjoyment of Jagmohan Das over the property was postponed; but in lieu of this enjoyment he obtained interest at 6 per cent. on the amount calculated as security. This was clearly his "Income". The learned Counsel for Jagmohan Das has argued that although it was his income income-tax is not assessable thereon because it consisted of receipts which were not receipts arising from business or the exercise of a profession, vocation or occupation and which were not by way of addition to the remuneration of an employee and which were of a casual and non-recurring nature. He asks us to apply the provisions of section 4, Cl. 3 (vii). The receipts in question were certainly not receipts arising from business or the exercise of a profession, vocation or occupation, nor were they by way of addition to the remuneration of an employee. But they were not of a casual and non-recurring nature. In these circumstances the exception does not apply and they are assessable to income-tax. We therefore answer the first question in the affirmative.

In respect to the second question we find that the income received in 1925-26 which has escaped assessment to income-tax comes within the scope of section 34 of the Act. We therefore answer the second question in the affirmative.

The third question is based upon a plea by the assessee that he should be allowed in reduction of his assessment the expenses of the litigation incurred in the suit with Indar Prasad. He is not entitled, in our opinion, to any reduction of assessment for this reason. The Income-tax Officer has not in any way taken

into account the capital which he gained out of that litigation. He has only taken into account the income which he derived on the capital which he obtained through that litigation. We therefore answer the third question in the negative.

The fourth question is a simple one. We are asked to set aside the proceedings on account of an irregularity. We do not find that there was any irregularity and we answer the fourth question in the negative. The assessee must pay the costs of this case. We fix the fee of the Government Advocate at Rs. 250; Rs. 100 has been received already. There will further be the costs of printing as certified by the Government Advocate and costs incurred in processes, etc.

(263) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

*Before Sir Murray Coutts Trotter, Kt., Chief Justice, Mr. Justice Beasley and
Mr. Justice Mackay.*

(19th September, 1928)

T. P. Pethaperumal Chettiar

Assessee.*

v.

The Commissioner of Income-tax, Madras.

Referring Officer.

Income-tax Act (XI of 1922), Secs. 4 (2) and 10 (2) (iii)—Computation of foreign profits—Tavanai loans—Interest in respect of previous years tavanai periods adjusted in account year—Deductability—Tavanai system, incidents of.

On an assessment under Sec. 4 (2) of the Income-tax Act, the assessee a money lender claimed that in the computation of his foreign profits interest due on Tavanai loans at the expiry of the tavanai periods in the previous years adjusted as having been paid in the account year should be deducted as an allowance under Sec. 10 (2) (iii) of the Act. On the claim being disallowed by the Income-tax Officer.

HELD, that the interest disallowed must be deemed to have been paid at the end of the respective tavanai periods in the years previous to the account year and added to the principal and hence not a permissible allowance in the account year.

Under the Tavanai system interest when not demanded is to be added to the deposit as an increase thereto.

Case (O. P. No. 129 of 1928) stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

CASE.

I have the honour to refer the following case for the opinion of the Hon'ble the Judges of the High Court under section 66 (2) of the Indian Income-tax Act, 1922.

2. The applicant is a Nattukottai Chetti residing at Shanmuganathapuram in the Ramnad district within the jurisdiction of the Income-tax Officer, First circle, Karaikudi. He has rubber gardens and money lending business at Taiping and the Federated Malay States.

3. In the year Krodhana (1925-26) he received a sum of Rs. 55,423 in British India from his business at Taiping, and in the course of the assessment proceedings of 1926-27 the question arose whether this sum, or any part of it, represented profit of the Taiping business liable to tax under section 4 (2) of the Act.

4. The Income-tax Officer examined the accounts of that business, computed the profits for the year of account Krodhana (12—4—25 to 12—4—26) to be \$22,820 or Rs. 35,257 and taxed this sum as profit remitted to British India. In computing the profits he disallowed a sum of \$13,301 claimed as expenditure of the year in the following circumstances.

5. The applicant had borrowed money from certain Nattukottai Chetti firms and the accounts showed that these loans had been taken on “3 months *tavanai*”. In the course of the year Krodhana four of these *tavanai* periods terminated and the total amount of interest that fell due on these four occasions was \$9,272. This sum the Income-tax Officer allowed as a deduction. But the applicant claimed in addition the above sum of \$13,301 consisting of interest which had fallen due on the expiry of previous *tavanai* periods. The income-tax Officer held that this interest must, in view of the character of the loans, be regarded as having been paid in previous years, and could not be treated as expenditure of the year, Krodhana. This decision was confirmed on appeal by the Assistant Commissioner. A copy of his order is appended (Exhibit A*).

6. In the accounts maintained by the applicant the whole sum of \$22,573 is adjusted as having been paid to the creditors in the year Krodhana. Corresponding entries showing receipts of the interest were made in the accounts of some of the creditors. It is admitted that these entries are not a record of cash payments. But the applicant claims that they prove an agreement between him and his creditors to pay and receive the whole of the accumulated interest in the year Krodhana and that there was in consequence a constructive payment of the whole sum in that year.

7. The accounts of the applicant have not been systematically maintained on any recognised basis, but the Assistant Commissioner has found that they are maintained on the mercantile system so far as these transactions are concerned. This finding is an inference from the nature of the loans themselves.

8. The applicant has required me under section 66 (2) of the Income-tax Act to refer certain questions of law for the decision of the High Court. The question arising for decision upon the above facts is the following and I refer it for the opinion of the High Court:—“Whether the sum of \$13,301 is allowable in this case as a deduction under section 10 (2) (iii) of the Income-tax Act as interest paid in the year Krodhana.”

9. The clause referred to allows as a deduction in respect of borrowed capital “the amount of the interest paid”; and in sub-section 3 we are informed that the word “paid” means “actually paid or incurred according to the method of accounting upon the basis of which the profits or gains are computed under

this section.” The applicant claims that his accounts are maintained according to what is known as the cash system; in other words that entries are made therein only when there is an actual payment or receipt of money. That this is not entirely accurate is clear from a passage in the appellate order passed by the Assistant Commissioner which I quote. “The Income-tax Officer reports that the appellant has not been following any regular system of accounting and that in some cases he (the appellant) has paid interest in cash without calculating and crediting the amount of interest in the account books and that in some others interest has been calculated and credited in the account books without any cash having been paid”. In the light of these facts it is hardly unfair to hold that the applicant has followed no regular system of accounting, and that in view of this the Income-tax Officer was entitled to exercise the discretion vested in him by section 13 of the Act. He cannot be said to have exercised that discretion unreasonably in refusing to allow more than one year’s interest. On that view of the case no question of law, would, I submit, arise. This was not, however, the ground taken by the Assistant Commissioner and I proceed accordingly to deal with the question of law which undoubtedly arises out of his order on the appeal.

10. It is not disputed that the loans interest on which is claimed as a deduction were advanced to the applicant on what is known as the *tavanai* system. *Tavanai* means a period of rest, and the distinguishing feature of such loans is that at the close of each period (in this case a period of 3 months) the interest due, if payment in cash has not been demanded by the creditor, is added on to the principal sum lent, and becomes merged in it, and begins to bear interest as part of such principal. The High Court of Madras has held in *Narayanan Chetty v. Suppiah Chetti*(1) that the amount thus added to the principal at the end of the *tavanai* period ceases subsequently to be “money payable for interest” within the meaning of Article 63 of the Limitation Act but that it has in fact become an increment to the deposit. When a loan of this kind is made, therefore, there is an implied agreement between debtor and creditor that the interest due shall be regarded as paid at the close of each period and lent again to the debtor. These payments of interest should be exhibited as such even in an account maintained on a cash basis, i.e., as a record of actual receipts and disbursement. The fact that the debtor and the creditors did not in this case make the necessary adjustments in their accounts at the end of each *tavanai* but made them subsequently cannot, I think, alter the real nature of the transaction or give rise to any inference that the payment was made at such subsequent time contrary to the terms of the original agreement. The sum of \$13,301 represented interest for *tavanais* prior to the year of account and must be taken to have been paid as it fell due. I am therefore of opinion that the Income-tax Officer was right in not allowing it as a charge against the profits of the year of account.

R. Kesava Iyengar, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

The question referred to us by the Commissioner of Income-tax, Madras, is “whether the sum of 13,301 Dollars is allowable in this case as a deduction under section 10 (2) (iii) of the Income-tax Act as interest paid in the year *Krodhana*” Under section 10 profits and gains of a business carried on by

(1) (1918) 43 Mac, 629.

an assessee are to be computed after making certain allowances and sub-clause (iii) allows the deduction of interest paid in respect of capital borrowed for the purposes of the business. The assessee is Nattukottai Chetty residing in the Ramnad District and has rubber gardens and a money lending business at Taiping in the Federated Malay States. In the year Krodhana (1925-26) he received a sum of Rs. 55,423 in British India from his business at Taiping and in the course of the assessment proceedings of 1926-27 the question arose whether this sum or any part of it represented profits of the Taiping business liable to tax under section 4 (2) of the Indian Income-tax Act. The Income-tax Officer examined the accounts of the Taiping business and computed the profits for the year of account Krodhana (13-4-1925 to 12-4-1926) to be 22,820 dollars and taxed this sum as profit remitted to British India. The assessee claimed an allowance of 22,573 dollars as expenditure in the business for that year, and under the following circumstances. The assessee had borrowed money from certain Nattukottai Chetty firms and the accounts showed that these loans had been taken on "3 months *tavanai*" and this is conceded by the assessee. In the course of the year of account four of these *tavanai* periods terminated and the total amount of interest that fell due on those four occasions was 9272 dollars. This sum the Income-tax Officer allowed as a deduction but the assessee claimed in addition the sum of 13,301 dollars which represented the interest which had fallen due on the expiry of previous *tavanai* periods. It is admitted that those *tavanai* periods expired in previous years or at any rate in the year previous to the year of account. The Income-tax Officer held that this interest, in view of the fact that these were *tavanai* loans, must be regarded as having been paid in previous years and could not be treated as expenditure of the year of account. He accordingly disallowed the assessee's claim with regard to 13,301 dollars. In the accounts maintained by the assessee the whole of the sum of 22,573 dollars which represents the interest due on the expiry of all *tavanai* periods including those of the previous years is adjusted as having been paid to the lenders in the year of account. Corresponding entries showing the receipt of interest were made in the accounts of some of the lenders. It is admitted that these entries are not a record of cash payment but they are used by the assessee to prove an agreement between him and his lenders to pay and receive the whole of the accumulated interest of the previous year in the year of account and that there was in consequence a constructive payment of the whole sum in that year.

We think it is perfectly clear that in order to claim an allowance in respect of interest paid on borrowed capital it must be paid in cash which is the cash basis of accounting, or it may be by adjustment which is the mercantile basis of accounting. No regular basis of accounting seems to have been adopted by the assessee but in any case, in our view, it does not matter what method was adopted because the whole question depends upon what the arrangement was between the assessee and the persons who advanced the money at the time of its advance. It is conceded that the money upon which the interest was due to be paid was advanced to the assessee on what is known as the *tavanai* system; and the learned Commissioner in his reference to us states as follows: "*Tavanai* means a period of rest, and the distinguishing feature of such loans is that at the close of each period (in this case a period of three months) the interest due, if payment in cash has not been demanded by the creditor, is added on to the principal sum lent, and becomes merged in it, and begins to bear interest as part of such principal". In *Narayana Chetty v. Subbayya Chetty*(1) it was held that such an arrangement

(1) (1918) 48 Mad. 629.

as this is a deposit and when interest is not demanded the interest is to be added to the deposit as an increase to the deposit. That means that the interest though not demanded is to be treated as paid and received and is to be added to the deposit itself to carry interest. The Income-tax Officer has therefore treated the interest due at the end of these tavanai periods as interest paid and he has adopted the same principle for both the year previous to the year of account and the year of account itself and has given the assessee the deduction allowable in respect the tavanai periods ending in the year of account. But since the tavanai periods in respect of which the assessee claims the allowance of 13301 dollars ended not in the year of account but in the year previous to it it must be taken similarly that the interest was paid by the assessee in that previous year and added to the principal and therefore not having been paid in the year of account the Income-tax Officer was quite correct in disallowing the assessee's claim.

For these reasons we answer the question referred to us in the negative.

The Commissioner on this Reference will get his costs, viz., Rs. 250.

(264) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

(19th September, 1928).

Before Sir Murray Coutts Trotter, Kt., Chief Justice,

Mr. Justice Beasley and Mr. Justice Muckay.

Karuppiah Kangani alias Kumaravelu Ambalam .. Assessee.*

v.

The Commissioner of Income-tax, Madras .. Referring Officer.

Income-tax Act (XI of 1922), Sec. 4 (2)—Assessee migrating to Ceylon from British India—Keeping houses in Ceylon and British India—If resident of British India—Assessability of foreign profits, test for—Residence in British India when profits arose.

The assessee, a native of British India, having migrated to Ceylon many years ago was living with his wife and children in a house on his estate there carrying on a prosperous business. He had another house in his native village where his second wife and children were living and where he owned lands, carrying on a small money lending business through a local agent. He was frequently visiting the village except during the period of October 1924 to October 1927. On an assessment to income-tax for the years 1925-1926, 1926-1927 and 1927-1928 of three sums of money as remittances of foreign profits of the years 1922-1923, 1923-1924 and 1924-1925 under Sec. 4 (2) of the Income-tax Act.

HELD, (1) that the assessee having been physically present in British India at the times when the profits sought to be assessed arose in Ceylon, they were assessable irrespective of the assessee's residence at the time of receipt or during the year of assessment.

(2) that on the facts of the case, the assessee could properly be described as residing in British India.

Case (O. P. Nos. 130, 131 and 132 of 1928) stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

* (1928) 55 M. L. J. 844; 29 L. W. 61; A. I. R. (1929) Mad. 35.

CASE.

I have the honour to refer the following case for the opinion of the Hon'ble the Judges of the High Court under section 66 (2) of the Income-tax Act, XI of 1922.

2. The applicant is a native of Kakkattiruppupudur in the Ramnad district within the jurisdiction of the Income-tax Officer, Karaikudi (Second Circle).

3. He migrated to Ceylon many years ago and he now owns tea estates and factories and carries on money lending and other businesses there. He has a house on one of his estates and his wife and children reside there.

4. He has a second house at Kakkattiruppupudur in which his second wife and his children by her are living. He has lands in the neighbourhood and he carries on money lending business there on a small scale. Up to the year 1924-25 he frequently visited his native village. His last visit was one of about two months in the period August to October 1924.

5. For the year 1926-27 the Income-tax Officer, Karaikudi assessed him on an estimated income of Rs. 60,400 under section 23 (4) of the Income-tax Act for failure to file a return of his income and produce his accounts. He reopened the assessment under section 27 on an application presented by Ramanuja Ayyangar, authorised agent of the present applicant. The agent filed a return of income showing an income of Rs. 1,890 from local money lending. In a memorandum appended to the return he stated that the applicant being a resident of Ceylon was not liable to be taxed on profits derived from his business in Ceylon and remitted by him to British India. The Income-tax Officer held that the applicant was a resident of Kakkattiruppupudur though he had a second residence in Ceylon. On an examination of the accounts the Income-tax Officer found that the applicant had the following profits at his disposal:—

Money lending and other business:—

				Rs.
1922-23	...	...	..	7,450
1923-24	...	...	..	18,505
1924-25	...	...	..	12,219
				<u>38,174</u>
<i>Tea:—</i>				
1924-25	...	...	..	92,264
				<u>1,30,438</u>

Out of this a sum of Rs. 51,639 had been taxed in the assessment of the year 1925-26. The balance of profits that accrued to the applicant at Ceylon during the years 1922-23 to 1924-25 and available for remittance during the year of account 1925-26 amounted to Rs. 78,799. The accounts showed that the applicant had received a sum of Rs. 4,798 in British India in that year. The Income-tax Officer held that the applicant had received that sum from out of those profits and assessed him on an income of Rs. 7,088 made up as follows:—

Property	...	...	..	Rs. 100
<i>Business:—</i>				
Kakkattiruppupudur		1890		
Ceylon profits remitted to British India.		4798	..	6,688
				<u>7,088</u>

6. On appeal the Assistant Commissioner agreed with the Income-tax Officer that the applicant was liable to be taxed on his foreign profits remitted to this country, but reduced the assessment under the head "Property" from Rs. 400 to Rs. 200.

7. The applicant has required me to state a case to the High Court and refer certain questions of law which he alleges arise out of the Assistant Commissioner's order. I think that the only question of law that arises is the following and I refer it for the decision of the High Court—“Whether in the circumstances of this case the sum of Rs. 4,798 can be lawfully taxed under the provisions of sub-section 2 of section 4 of the Indian Income-tax Act as having accrued and arisen without British India to a person resident in British India.”

8. It is contended on behalf of the applicant that having been assessed through an agent under section 40 on the ground of non-residence, he cannot be treated in the assessment as a "person resident in British India" within the meaning of section 4, sub-section (2). The facts (i) that the applicant was residing out of British India when the assessment was made upon him, and (ii) that he was resident in British India when the profits accrued and arose, appear to be a sufficient answer to this charge of inconsistency.

9. Section 3 of the Income-tax Act (read with the annual Finance Act) imposes a tax on the income, profits and gains of the previous year of every individual. By sub-section (1) of section 4 the Act is made applicable subject to certain exceptions to all income, profits and gains accruing or arising or received in British India or deemed under the provisions of the Act to accrue or arise or to be received in British India. The tax is therefore payable on all income accruing or arising or deemed to accrue or arise in British India whether the recipient resides in British India or not. Under sub-section (2) of section 4 the profits and gains of a business accruing and arising without British India to a person resident in British India are, if they are received in or brought into British India within three years of the end of the year in which they accrued or arose, deemed to have accrued or arisen in British India and to be profits and gains of the year in which they are so received or brought. This clause does not require, as the applicant contends, that the assessee should be resident in British India at the time of assessment or during the year of remittance. It requires such residence only during the period in which the profits accrued. The profits that have been assessed in the present case accrued during the three years 1922-23, 1923-24 and 1924-25 and it is not disputed that the assessee was resident in British India during those years. I am therefore of opinion that the sum of Rs. 4,798 was rightly taxed under sub-section (2) of section 4.

V. V. Srinivasa Iyengar and K. S. Rajagopalachary, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.*

These are three references made by the Commissioner of Income-tax, under section 66 (2) of the Income-tax Act, (XI of 1922) at the instance of an assessee, Karuppiah Kangani *alias* Kumaravelu Ambalam.

* Delivered by Mackay J.

The assessee is a native of the village of Kakkattiruppupudur in the District of Ramnad. He migrated to Ceylon many years ago and prospered. He now owns tea estates and factories in that Island and carries on money lending and other forms of business in the Colony. He owns a house on one of the estates and there his first wife and her children live.

He has a second house in his native village in which his second wife and his children by her reside. He has land in the vicinity and carries on money-lending in that village on a limited scale; and he has a local agent to conduct his affairs. Up to the year 1924-25 he frequently visited Kakkattiruppupudur, his last visit at that period being from August to October 1924. His next visit was in October 1927 and it would appear that from that date he continued to reside there until the date of the reference in O. P. No. 131 of 1928, 11th April 1928.

The common question of law referred for adjudication is whether in the circumstances of these cases the assessee can be lawfully taxed under the provisions of sub-section 2 of section 4 of the Income-tax Act in respect of three different sums as having accrued or arisen as profits and gains of a business without British India to a person resident in British India. These sums were, in O. P. No. 130 of 1928, Rs. 21,639 (or perhaps more accurately, Rs. 51,639); in O. P. No. 132 of 1928, Rs. 4,798; and in O. P. No. 131 of 1928, Rs. 62,291.

We agree with the decision in *Behari Lal Mullick v. Commissioner of Income-tax, Bengal*(1) that, under the Indian Income-tax Act, XI of 1922, the income of the year previous to the year of assessment is not to be taken as merely a guide to the ascertainment of the income of the year of assessment, but as the actual sum which is subject to taxation. This seems clear on the language of section 3 of the Income-tax Act, XI of 1922, and differentiates the cases under the Indian Act from those under the English Act, so that *Brown's case*(2) is not an authority that binds us.

In O. P. No. 130 of 1928 the profits and gains sought to be taxed accrued or arose outside British India during the periods 1922-23, 1923-24, and 1924-25 when the assessee resided at different times in British India, the profits and gains were remitted to British India in 1924-25 during which period he was resident therein; the year of assessment was 1925-26, when he was not resident.

In O. P. No. 132 of 1928 the profits and gains accrued or arose outside British India in 1922-23, 1923-24 and 1924-25 when the assessee was resident in British India as stated above; they were received in British India in 1925-26 when also he was not resident.

In O. P. No. 131 of 1928 the profits and gains accrued or arose outside British India in 1924-25 when the assessee was for part of the period physically resident in British India; they were received in British India in 1926-27 when he was not so resident; the year of assessment was 1927-28 when he was so resident.

That brings the question we have to decide down to this short point: Was the assessee a resident within the meaning of the statute in British India at the material dates which we think must be taken to be the dates when the profits

(1) 2 I. T. C. 328 ; 54 Cal. 640.

(2) 8 Tax. Cas. 57 ; (1921) 2 A. C. 22.

and gains sought to be taxed accrued to the assessee in Ceylon (Income-tax Act, XI of 1922, section 4 (2)). There can be no doubt as to what the answer must be: in all the three cases before us he was physically present in British India at the time when the profits sought to be taxed accrued in Ceylon; though in two of the cases he was not physically present in British India when the remittances were received; and in two similarly he was not physically present during the year of assessment. But we entertain no doubt that he could properly be described as "residing" here: he owned a house in the Ramnad district where his second wife and her children by him lived and he stayed in that house whenever he came to British India. The assessee will pay the costs of these references Rs. 250 consolidated for all three.

(265) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Sir Murray Coutts Trotter, Kt., Chief Justice,

Mr. Justice Beasley and Mr. Justice Reilly.

(26th October, 1928).

M. V. Krishna Aiyer & Sons

.. Assessee.*

v.

The Commissioner of Income-tax, Madras

.. Referring Officer.

Income-tax Act (XI of 1922), Sec. 2 (14)—Partnership deed for a term—Expiry of term during account year—Subsequent continuation without fresh deed—Firm, if registrable—Registration Rules, Rule 2.

The partners of a firm constituted in August 1923 under a partnership deed for a term of three years continued the partnership after the expiry of the term without any fresh deed. For the assessment year 1927-1928, a return of income of the previous year 1926-1927 was submitted together with an application for registration of the firm under Sec. 2 (14) of the Income-tax Act. On a refusal of registration by the Income-tax authorities

HELD, that the contractual nexus between the partners after the expiry of the original term being a new implied oral agreement, there was no instrument of partnership operative at the time of the application which could be registered under Rule 2 of the Registration Rules and that it was immaterial that the term expired in August 1926 after the lapse of some months in the account year 1926-1927.

Clarke v. Leach, 1 De. G. J. & S. 144 and Nellson v. Mossend Iron Co., 11 App. Cas., 298, Applied.

Case [O. P. No. 133 of 1928] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

CASE.

I have the honour to refer the following case for the opinion of the High Court under section 66 (2) of the Income-tax Act.

* (1929) I. L. R. 52 Mad. 367 ; 56 M. L. J. 151 ; 29 L. W. 103 ; A. I. R. (1929) Mad. 67.

2. The applicants are a firm of silk merchants. They were called upon under section 22 (2) of the Act to make a return of their income of the previous year with a view to assessment in the year 1927-28. They submitted the return on 26th July, 1927, and at the same time applied for registration under Rule 4 of the rules framed under the Act. In compliance with Rule 2, they produced partnership deeds dated 3rd November, 1917, and 29th August, 1923. True copies of these deeds (Exhibits A* and B*) and English translations thereof (Exhibits A-1* and B-1*) are appended to this reference. The Income-tax Officer found that the object of the later deed (Exhibit B) was to continue the partnership created in the earlier deed (Ex. A) for a period of three years from 31st August, 1923, that this period had expired on or about 30th August, 1926, and that no further deed had been executed to prolong the life of the partnership beyond that date. In these circumstances he rejected the application and assessed the applicants as an unregistered firm. The applicants appealed unsuccessfully to the Assistant Commissioner, a copy of whose order is enclosed (Ex. C*).

3. The question arising in the case, on which the opinion of the Court is solicited, is whether the applicants were entitled to be registered by the Income-tax Officer under Rule 4 of the rules framed under the Act.

Sub-section 14 of section 2 of the Act defines "registered firm" as a "firm constituted under an instrument of partnership specifying the individual shares of the partners of which the prescribed particulars have been registered with the Income-tax Officer in the prescribed manner." "Prescribed" according to sub-section 10 of the same section, means "prescribed by the rules made under this Act". Rules 2 to 6 of the rules made under section 59 of the Act prescribe the manner in which the registration may be applied for and effected. According to Rule 2, "any firm constituted under an instrument of partnership specifying the individual shares of the partners" may apply for registration. According to Rule 3, the application "shall be accompanied by the original instrument of partnership under which the firm is constituted together with a copy thereof."

4. The application under Rules 2 and 3 was made in this case on 26th July 1927. The period of three years specified in the deed Ex. B having expired nearly a year previously I submit that the applicants were not, on 26th July 1927, a firm constituted under an instrument of partnership and were not therefore competent under Rule 2 to apply for registration. I submit further that, since the deed produced was not one under which the firm was then constituted, the conditions of Rule 3 were not satisfied.

5. The applicants rely on section 256 of the Indian Contract Act, the effect of which, according to them, is that on 26th July, 1927, the deed—Ex. B—was still in force although the period of three years mentioned in it had expired. That section runs as follows:—"If a partnership entered into for a fixed term be continued after such term has expired, the rights and obligations of the partners, will, in the absence of any agreement to the contrary, remain the same as they were at the expiration of the term, so far as such rights and obligations can be applied to a partnership dissolvable at the will of any partner."

6. My opinion is that the applicants have mistaken the effect of this section. When a document creating a partnership of a specific period has

ceased to have effect owing to the expiry of the period and no fresh document has been executed, the partnership may, no doubt, continue, but it cannot be said to continue under the instrument. The continuance is a result of a new agreement which is not identical with that embodied in the instrument, although some of its terms are presumed to be in accordance therewith.

In my opinion, therefore, the Income-tax Officer's decision was correct and the question should be answered in the negative.

K. S. Krishnaswamy Ayyangar and R. Rajagopala Ayyangar, for the Assessors.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

CHIEF JUSTICE:—This is a reference put up by the Commissioner of Income-tax under section 66 of the Act. The question on which our opinion is asked is whether in such circumstances as this case discloses the assessee was entitled to be registered under Rule 4 of the Rules framed under the Act. I will briefly summarise what the material circumstances are in this case. The original partnership was entered into by deed on the 3rd November 1917, the contracting parties being Venkatarama Aiyer and Sons of the one part and D. Krishnaswami Aiyangar of the other. The business they carried on was that of silk merchants and the term of the partnership deed was expressed to be for five years, so that it expired on the 3rd of November 1922. On the 31st of August 1923, a new partnership deed came into effect for a period of 3 years, so that it would expire on the 31st of August 1926. In fact the business was continued thereafter by the partners as before for aught we know down to this day. A return was called for by the income-tax authorities for the year, April 1926—April 1927, for the purposes of assessment. That return was made and besides the return on the 26th of July 1927, the assessee put in an application for registration of the firm. The Commissioner has refused to register the partnership for the purposes of the Act and the question is, whether he was right.

I will now shortly refer to the two or three material sections and rules of the Income-tax Act. By section 2 (14) "A 'registered firm' means a firm constituted under an instrument of partnership specifying the individual shares of the partners of which the prescribed particulars have been registered by the Income-tax Officer in the prescribed manner" and the manner is prescribed in the rules. The material rule is Rule 2 which runs as follows:—"Any firm constituted under an instrument of partnership specifying the individual shares of the partners may for the purposes of clause 14 of section 2 of the Indian Income-tax Act register with the Income-tax Officer particulars contained in the said instrument on application in this behalf made by the partners or any of them" and then follows a form which sets out the particulars which are to be given. This form was filled in and the application was accompanied by a copy of the instrument of partnership of the 31st of August 1923. The Commissioner bases his refusal to register the particulars forwarded by the assessee firm on the ground that, when the application for registration was made the instrument of partnership had ceased to be operative, that the partnership was at that date being carried on under what must be regarded as a new agreement which, being verbal, could not be said to be an instrument of partnership within the meaning of the rules. The contention of the assessee is that the true view of the position was that the business was by verbal arrangement or tacit consent between the partners being carried on under the original instrument

of 31st August 1923 whose life had been prolonged and continued by the act of the parties. The dividing line no doubt is a very narrow one and language is used from time to time in the English authorities which speaks of a contract to renew by implication and it is said that that enabled the partnership whose life had been continuous since the deed of 1923 to have it registered as the document governing their relations throughout. In one sense there clearly was no new partnership here in the sense, that is, that there was no change in the personal and that the trading carried on was continuous without break from August 1923.

The real question we have to determine is whether in contemplation of law the original contract was actually continued in existence or whether the true view is that such of its terms as could be taken to govern the subsequent period could only do so on the footing that they were impliedly revived, in so far as they are applicable to the partnership at will, by the tacit verbal agreement which is to be regarded as arising from the continuance of the trade thereafter. We think that there are two decisions of the House of Lords which conclude this question in favour of the Crown. The first is a decision of Westbury L.C., *Clarke v. Leach* (1), and the Lord Chancellor says this:—"Ordinarily a contract for a term constituted by a written agreement must be considered as having come to an end at the expiration of the period for which it was entered into; and the contract during the term differs from that which arises from the continuance of the relation by the mutual consensus of the parties after the term has expired. The one is to last for a certain term; the other only for so long a time as they both shall choose. Am I then by any principle of law bound to assume or justified in assuming that all the special articles and conditions in the original written deed of partnership for a term are at once transferred by law to this new contract, which has no particular limit to the term of its duration? That would be a strong and extravagant assumption, and one that is not warranted by any principle or authority."

That passage appears to me to make it clear that Lord Westbury considered the contractual *nexus* of the parties after the expiry of the deed to rest upon the new implied oral agreement, and that the articles of the deed which are to be considered as preserved are preserved not by virtue of the original deed which had ceased to operate but of the new agreement. In the case of *Nelson v. Mossend Iron Co.* (2), Lord Selborne puts the matter thus: "There is no doubt about the law that, when there is a partnership for a term of years, and it is afterwards, after the expiration of the term, continued at will, the rule, in the absence of a contract to the contrary, is that it may be presumed that the new business is carried on upon the old terms as far as they are applicable to it, and only so far; and as far as the principle is concerned, I do not think there is any discrepancy between any of the authorities. It is not at all necessary to examine into the particular cases in which it has been held that a particular term of a written contract did or did not go into the new and unwritten contract, because every case has turned upon its own particular circumstances and upon the question as applied to the words of the particular instrument, whether the old term was or was not applicable to the new contract."

Similar language is used by Lord Watson who speaks specifically at page 308 of a distinction between the 'old' contract, and the 'new'. And the new contract is none the less a new contract, we must take it, because it by implication contains within itself certain terms of the old written contract, as

(1) 1 De G. J & S. 44.

(2) 11 App. Cas. 293.

it were re-enacted. These pronouncements of the highest tribunal do not turn on any special provision of any statute but are based on the general principles of the law of partnership and we should, we think, endeavour respectfully to follow those high authorities. I think that there is nothing in the language of section 256 of the Indian Contract Act which, in any way, modifies the effect of those decisions of the House of Lords. The result is that at the time that the assessee applied for registration there was no operative document to be registered.

Another short contention is raised and that is this. The year of assessment with which we are concerned is the year 1927-28 and it is said that as that will be a return of trading profits for the year 1926-27 registration ought not to have been refused as four months of that trading year were before the expiration of the deed of the 31st of August 1923. We cannot accede to this contention. What we have to look to is the year of assessment; and had the application of the 21st of July 1927 been granted it would still in our opinion only apply to the financial year 1927-28. On these grounds we think that the Commissioner was right in rejecting the application for registration and that we must so answer the questions submitted to us and order the assessee to pay the Government Rs. 250 as the costs of this reference.

My learned brothers have seen this judgment and agree with it.

(266) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

(5th November, 1928).

*Before Sir Murray Coutts Trotter, Kt., Chief Justice, Mr. Justice Beasley
and Mr. Justice Reilly.*

...
R. M. S. R. M. Ramaswami Chettiar ... Assessee.*

v.
The Commissioner of Income-tax, Madras ... Referring Officer.

Income-tax Act (XI of 1922), Secs. 22 (4), 23 (2) and (4)—Submission of return by assessee—Subsequent notice under Sec. 22 (4) to produce accounts—Asst. under 23 (4) on non-production, legality of.

The assessee called upon to adduce evidence in support of his return under Sec. 23 (2) of the Income-tax Act produced some evidence. Finding it to be insufficient, the Income-tax Officer issued a notice under Sec. 22 (4) calling for the production of certain account books and on non-production of the same made an assessment under Sec. 23 (4).

HELD that the Income-tax Officer had power under Sec. 22 (4) to call for accounts after submission of return and on the assessee's non-compliance to make an assessment under Sec. 23 (4).

Harmukhrai Dulichand v. Commissioner of Income-tax, Bengal 3 I.T.C. 198; Ramkelawan Ugamlal v. Commissioner of Income-tax, Behar and Orissa 3 I.T.C. 225; Chandra Sen Jaini v. Commissioner of Income-tax, U. P. 3 I.T.C. 17, Followed.

Cases (O. P. Nos. 186, 187 and 188 of 1928) stated under Sec. 66 of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

* (1929) 1. L. R. 52 Mad. 194; 56 M. L. J. 141; 29 L. W. 273; A. I. R. (1929) Mad. 60.

CASE.

In pursuance of the order quoted above, I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (3) of the Income-tax Act.

2. The petitioner is a resident of Karaikudi within the jurisdiction of the Income-tax Officer, First Circle, Karaikudi. He is the proprietor of a banking business at Kiddah and is also a partner in another banking business at Tapah, both situate in the Federated Malay States.

3. For the assessment of the year 1926-27 (based on the income of the Tamil year Krodhana) the petitioner returned an income of Rs. 125 from property and stated that he had received a remittance of Rs. 4,050 from his Kiddah business. He added that there were no profits in that business and that the remittance received by him was from his capital there.

4. By a notice issued under section 23 (2) of the Income-tax Act, the Income-tax Officer called on the petitioner to adduce evidence in support of his return. The petitioner produced some of the extracts of accounts received from his Kiddah business, but not all, i.e., the extracts up to Karthigai Krodhana (November 1925) in respect of one agency and all the extracts in respect of the other.

5. During the year of account the petitioner maintained two sets of books for his Kiddah business, one for the agency of Sathappan which ended in about Thai of the year of account and the other for the subsequent agency which began from Avani Krodhana (August 1925), i.e., in the middle of the year of account. According to the accounts produced a profit of \$77,818 accrued to the petitioner in Sathappan's agency. The old agency-Sathappan's agency—ended in Thai Krodhana (February 1926); but the accounts produced stopped with Kartigai Krodhana and it was evident from the extracts produced that the accounts had not been finally closed by that date. For instance, there was a cash balance of \$29,363 in the old agency accounts which had not been brought forward in the new agency accounts or otherwise accounted for. Further, a sum of \$41,000 was found debited to the personal accounts of the petitioner, i.e., withdrawn by him from the Kiddah business for investment elsewhere.

6. The evidence produced by the petitioner was therefore in the opinion of the Income-tax Officer insufficient to prove the amount of his income. He therefore issued a notice under section 22 (4) calling for the complete accounts of the closed agency at Kiddah and also for documents to prove that the money withdrawn from the Kiddah business did not represent profits received in British India. The date fixed for the compliance with this notice was 3rd July 1926 and the notice was served on the petitioner's undivided son, who assists him in the business and was formerly himself the petitioner's agent at Kiddah. On 3rd July the petitioner's clerk appeared without the accounts specified. He offered to get certain "extracts" from the day books maintained at Kiddah if two months' time was allowed. The Income-tax Officer had reason to believe that the accounts called for could have been produced if the petitioner had so desired. He therefore held that the petitioner failed to comply with the terms of the notice issued under section 22 (4) and made an assessment under section 23 (4).

7. The petitioner applied to the Income-tax Officer to re-open the assessment under section 27, but without success. A copy of the Officer's order is filed, marked Exhibit A.*

* Not printed.

8. The petitioner appealed to the Assistant Commissioner against the order of the Income-tax Officer with a like result. A copy of the Assistant Commissioner's order is filed, marked Exhibit B.*

9. The petitioner then filed a petition before me under section 66 (2) of the Income-tax Act and required me to state a case and refer certain questions for the decision of the High Court. I declined to do so on the ground that no question of law arose for decision, except the one that I have been directed to refer in the High Court's order quoted above. This question had already been referred to the High Court in the case of P. Thiruvengada Mudaiar (Referred Case No. 3|27) and I undertook to give the petitioner any relief to which he might be entitled as a result of the decision on the question. A copy of my order is enclosed, marked Exhibit C.*

The petitioner thereupon moved the High Court under section 66 (3) of the Income-tax Act and in its order dated 9th December 1927, the High Court has directed me to state a case and refer the following question:—"The applicant having made a return of his income and having complied with the terms of the notice issued to him under section 23 (2), was there any jurisdiction in the Income-tax Officer to revert to section 22 (4) and make an assessment under section 23 (4) for non-compliance with the notice under section 22 (4)".

10. The contention underlying this question appears to be two-fold. It is suggested, in the first place, that when once a return of income has been made an Income-tax Officer's power to issue a notice under sub-section 4 of section 22 calling for accounts or documents is at an end; and, secondly, that even if the issue of such a notice after the receipt of a return is legal, the person who fails to comply with the terms of the notice so issued may not, on this ground, be assessed under sub-section 4 of section 23, and deprived of his right of appeal.

Little need be said regarding the first branch of this argument. The language of sub-section 4 of section 22 is unambiguous. Only one condition is there imposed on the Officer's power to issue the notice and that condition is that the person to whom it is issued must be either a company or a person upon whom a notice under sub-section 2 of this section has been served. It is clear, that, if the legislature had intended to impose other conditions, it would have stated these in the sub-section itself, and would not have left them to be inferred from words used in a different section altogether, or from the mere order of sequence of the sections. If, however, evidence regarding the intention of the legislature is to be looked for outside the Act, it will be found in the report of the All-India Income-tax Committee of 1922 which says in paragraph 34 "We agree..... that a Collector" (now an Income-tax Officer) "should have power to call for the production of accounts whether a return has or has not been filed;" or in paragraph 14 of the Statement of Objects and Reasons appended to the bill of 1922: "The bill provides that the assessor" (now Income-tax Officer) "may call for accounts whenever he considers it necessary".

The second branch of the argument is based on the language of sub-section 4 of section 23. That sub-section runs as follows:—"If the Principal Officer of any Company or any other person fails to make a return under sub-section 1 or sub-section 2 of section 22, as the case may be, or fails to comply with all the terms of a notice issued under sub-section 4 of the same section or, having made a return, fails to comply with all the terms of a notice issued under

sub-section 2 of this section, the Income-tax Officer shall make the assessment to the best of his judgment". It is suggested that if the words "having made a return" are not mere surplusage, the meaning of the latter part of this sub-section must be as follows:—"If a person, not having made a return, fails to comply with all the terms of a notice issued under sub-section (4) of section 22 or, having made a return, fails to comply with all the terms of a notice issued under sub-section (2) of this section the Income-tax Officer shall make the assessment to the best of his judgment". Thus the words "having made a return" have to be read into the sub-section in order that it may bear the meaning attributed to it by the petitioner.

I submit that if the words "having made a return" necessarily imply an antithesis to something not expressed in the Act, the antithesis is between what may occur when a man has made a return and what may occur whether he has made a return or not; and that it would be more consistent with the other provisions of the Act to insert these words ("whether he has made a return or not") if any are to be inserted at all.

I submit, further, that if in construing this sub-section it is necessary to choose between treating certain words as superfluous and importing words into the statute, the former method is the less open to objection; and it is my considered opinion that, in this instance, the intention of the legislature could have been adequately expressed if the words "having made a return fails to comply with all the terms of a notice issued" had not been enacted. The words "having made a return" appear to have been carried over without sufficient consideration from sub-section (4) of section 18 of the Income-tax Act, VII of 1918, where they are used with more point, since there was no provision in that Act corresponding to section 22 (4) of the present Act. In both Acts these words appear to be more or less superfluous, but their presence can perhaps be justified on the view that they were inserted *pro majore cautela*, to emphasise the fact that, even when the party, by submitting a return, has avoided one of the defaults specified in the sub-section, he may still commit another, and thereby incur the same penalty, by subsequent failure to comply with a notice under section 23 (2).

In my opinion, therefore, the Income-tax Officer was entitled to issue a notice under sub-section (4) of section 22 in this case, and to assess under sub-section (4) of section 23 for failure to comply with that notice.

K. S. Krishnaswami Iyengar and R. Kesava Iyengar, for the Assessee.
M. Patanjali Sastri, for the Crown.

JUDGMENT.

O. P. No. 188 of 1928.

In this case an income-tax assessee made a return of his income when required to do so under section 22 (2) of the Indian Income-tax Act, 1922. Not being satisfied with the return the Income-tax Officer required the assessee under section 23 (2) of the Act to produce evidence in support of his return. The assessee produced some evidence; but the Income-tax Officer found it insufficient to show the amount of the assessee's income and then issued a notice to him under section 22 (4) of the Act to produce complete accounts of a branch business at a place in the Federated Malay States for the account year in question. Those accounts the assessee did not produce, and the Income-tax Officer therefore proceeded to make his assessment under section 23 (4) of the Act, that is, an assessment not made upon evidence but "to the best of his judgment", an assess-

ment from which under the Act the assessee had no right of appeal. The question referred to us is "The applicant having made a return of his income and having complied with the terms of the notice issued to him under section 23 (2), was there any jurisdiction in the Income-tax Officer to revert to section 23 (4) for non-compliance with the notice under section 22 (4)?" The assessee contends that in those circumstances the Income-tax Officer had no power to make an arbitrary assessment under section 23 (4) from which there was no right of appeal.

This question has been before 4 of the Indian High Courts. It has been answered against the assessee by a unanimous Full Bench of three Judges of the Calcutta High Court in *Harmukhrai Dulichand v. Commissioner of Income-tax, Bengal*(1), by a unanimous Full Bench of 5 Judges of the Patna High Court in *Liamkelawan Ugamlal v. Commissioner of Income-tax, Behar and Orissa*(2), overruling *Brij Raj Rang Lal v. Commissioner of Income-tax, Behar and Orissa*(3), a decision of 2 Judges and by a Division Bench of the Allahabad High Court in *Chandra Sen Jain v. Commissioner of Income-tax, United Provinces*(4). Now that the earlier decision of the Division Bench of the Patna High Court has been overruled there remains in the assessee's favour, of the cases quoted before us, only a decision of a Division Bench of the Lahore High Court in *Khushi Ram Karam Chand v. Commissioner of Income-tax, Punjab*(5). At one stage of the arguments before us it was suggested that the decision of a Full Bench of this Court in *Pitta Ramaswamiah v. Commissioner of Income-tax, Madras*(6), was by implication in favour of the assessee in this matter; but on examination it will be seen that it was found in that case that the assessment was in fact made, not under section 23 (4) but under section 23 (3). The weight of authority on the question before us is therefore overwhelmingly against the assessee.

It was first contended by Mr. Krishnaswami Ayyangar for the assessee that the Income-tax Officer's power to call for accounts under section 22 (4) can be exercised only before the assessee has submitted a return of his income. There is nothing whatever in the wording of the sub-section to suggest that. On the contrary the only limitations on the power of the Income-tax Officer to call for accounts in that sub-section are that, if the assessee is not a company, a notice requiring him to make a return of his income must have been served on him and that accounts for a period more than 3 years prior to the previous year cannot be called for. The fact that those restrictions are mentioned explicitly makes it the more improbable that any other restriction is implied. It is urged that the fact that the sub-section occurs in section 22, which deals with the procedure for getting in a return, makes it probable that all its provisions apply to the stage before the return comes in. That would be a very unsafe reason for limiting the plain effect of the words of the sub-section; and it may be remarked that sub-section 3 of section 22 enables the assessee to do something after he has submitted his return. If section 22 (4), is to be construed as in this part of his argument Mr. Krishnaswami Ayyangar would have us to construe it, we must read into it a very important restriction, which only a very careless Legislature could have omitted to express if it were intended. And, as has been pointed out by Mr. Pantanjali Sastri for the Commissioner of Income-tax, in the great majority of cases it must be after the return has come in, not before, that the Income-tax Officer has any need to see the assessee's accounts. If the provision for calling for accounts were restricted to the period before the return is submitted, it would be of comparatively little use. Until he knows whether a com-

(1) 3 I.T.C. 198.

(2) 3 I.T.C. 225.

(3) 2 I.T.C. 458

(4) 3 I.T.C. 17.

(5) 2 I.T.C. 517.

(6) 2 I.T.C. 196.

pany is going to submit its return by the 15th June or any other assessee going to submit his return by the date specified in the notice to him under section 22 (2), the Income-tax Officer need not trouble about accounts at all, as, if no return is submitted in time, he can, as is unquestioned, make his arbitrary assessment under section 23 (4) without referring to any accounts or evidence. It is very highly improbable that the only specific provision made by the Legislature for calling for accounts would apply to the period when accounts are least required. But it has been argued—and the argument was adopted in *Kushi Ram Karam Chand v. Commissioner of Income-tax, Punjab* (1) and in the overruled case in the Patna High Court—that this surprising restriction of the effect of section 22 (4) has been introduced by the Legislature in a cryptic and back-handed way by the wording used in section 23 (4). What the exact meaning of that wording is I will discuss later; but pushed to its furthest grammatical extreme, as contended by the assessee, it comes to no more than this—that the penalty provided by section 23 (4) for failure to produce accounts when required to do so by a notice under section 22 (4) applies only if the notice is issued before the return is submitted. Even if that interpretation were correct, it would in my opinion be a clearly insufficient reason for refusing to read section 22 (4) according to its plain meaning and for reading into it a remarkable and very important restriction which those who framed it could hardly have forgotten to express. The prevailing judgment of the Calcutta, Allahabad and Patna High Courts which I have mentioned, agree that there is no such restriction.

But Mr. Krishnaswami Ayyangar has tried to get at the same result by another road. In a later stage of his argument he has admitted that the Income-tax Officer must have a right to call for the assessee's accounts even after he has submitted his return but has suggested that calling for accounts at that stage is provided for in section 23 (3). The admission that the Income-tax Officer can call for accounts under section 23 (3) in the course of an inquiry under that sub-section Mr. Krishnaswami Ayyangar can make without reluctance because failure to comply with a demand of the Income-tax Officer made under that sub-section does not expose the assessee to the penalty of arbitrary assessment provided by section 23 (4). If the Act provided explicitly for calling for accounts during the inquiry under section 23 (3), which is to be made after a return has been submitted, there might be some reason for supposing that the provision for calling for accounts under section 22 (4) applied only to an earlier stage. But the power given to the Income-tax Officer by section 23 (3) is to require the production of evidence "on specified points". If it were intended by those words to give power to call for accounts for several years, the language would in my opinion be ill-chosen and misleading. If it were intended to give power to call for accounts, what object could there be in failing to say so explicitly, what object could there be in using language in such contrast with the language of section 22 (4)? The accounts of a series of years may provide evidence on a specified point; but to describe them as "evidence on a specified point" is obviously inappropriate. To my mind the language of section 23 (3) adds force to the Commissioner's contention. If accounts can be called for at any stage, before or after the return is submitted, then in the inquiry under section 23 (3) power to call for further evidence on specified points is enough and the language of that sub-section need not be strained in any way.

And, though Mr. Krishnaswami Ayyangar has called section 23 (3) to his aid as showing an implied restriction of section 22 (4), on examination it throws no light on the question of immediate importance in this case—whether failure to produce accounts when called for after a return has been submitted

entails the penalty of arbitrary assessment under section 23 (4). Failure to comply with a direction under section 23 (3) does not entail that penalty. If the power of the Income-tax Officer under section 23 (3) is confined to the plain meaning of that sub-section, viz., to call for evidence on specified points, it is reasonable that failure to comply with such a direction should not entail the very severe penalty of arbitrary assessment without right of appeal. If it did entail that penalty, it could obviously be used in a very oppressive way. For instance, the Income-tax Officer might call for some evidence of doubtful relevance and difficult or impossible to produce, and, if it were not produced, enforce the penalty of arbitrary assessment. That would be clearly unjust, and the Legislature has rightly made the penalty of arbitrary assessment inapplicable to such a case. But, if an assessee fails to produce at any stage when required his accounts—the most important of all evidence in such a matter the very evidence on which, if he is honest, he will himself wish to rely—why should he be treated more leniently when his improper and obstructive refusal comes after, instead of, before he submits his return. No reason has been suggested for such a distinction. On the contrary the man who refuses to produce his accounts when the Income-tax Officer has expressed under section 23 (2) dissatisfaction with his return is clearly more blame-worthy and obstructive than the man who fails to produce them before he has made his return, when no one has yet expressed an opinion whether his return will be an honest one or not. When once it is admitted that the Income-tax Officer must have power to call for accounts in the course of the inquiry under section 23 (3) and without it the inquiry might easily be reduced by the assessee to a farce—the omission to penalise failure to comply with the officer's requisition under that sub-section by arbitrary assessment is strong evidence that the right to call for accounts even at that stage must be found elsewhere, that is, in section 22 (4):

There remains the actual wording of section 23 (4) which sets out the failure on the part of the assessee which entails the penalty of arbitrary assessment without appeal. It is contended that, even if section 22 (4) gives power to call for accounts after the assessee has submitted his return, the penalty of arbitrary assessment is restricted to a failure to produce accounts when called for before the return is submitted. As I have indicated there is nothing in the object or nature of the proceedings and nothing in section 22 or the rest of section 23 to make it probable that the Legislature would intend to treat more leniently a failure to produce accounts when required after the submission of a return than before it. But it is contended that the wording of section 23 (4) has that surprising result. It is quite clear that, if a company or other assessee fails to submit a return by the proper date, the penalty of arbitrary assessment is to be enforced. That is what the sub-section first provides. Then it goes on to provide the same penalty for failure "to comply with all the terms of a notice issued under sub-section 4 of section 22". If the notice under section 22 (4) can be issued at any time—and that I do not think can now be doubted—there is nothing so far to suggest that the penalty is attached only to failure to comply with a notice issued under section 22 (4) before a return is submitted. But section 23 (4) goes on to provide that, if a company or other assessee "having made a return fails to comply with all the terms of a notice" issued under section 23 (2) the penalty shall apply. The contention of the assessee in this case rests upon the insertion of the words "having made a return". It is urged with truth that failure to comply with a notice under section 23 (2) can occur only after making a return as that notice cannot be issued before a return is made. Therefore it is contended these otherwise useless words must have been introduced to show by contrast that the other two

failures penalised must occur before a return is made. No such contrast could be of any use in regard to the first failure mentioned in the sub-section, which is failure to make a return at all. Then this supposed contrast, if it indicates anything, must be understood to indicate that the failure to comply with a notice to produce accounts under section 22 (4) is to be penalised only if the notice is issued before the return is submitted. But, if that was the intention, if the object was to express something of such importance, why try to indicate it in a clumsy and obscure way? We must all accept the principle adopted in *Kushi Ram Karam Chand v. Commissioner of Income-tax*(1), that, if two constructions of a fiscal enactment are equally possible and reasonable, the construction more favourable to the subject must be enforced. But the contention of the assessee in this case rests on too frail a foundation. The words "having made a return" in section 23 (4) may be superfluous and add nothing necessary for the description of the third failure penalised but they are applicable to that failure. Their use may be tautological and inartistic. But because they are unnecessary we are not justified in jumping to the conclusion that they have been used to express something which it cannot be pretended they could express clearly, which a child could express clearly in other words, which no man of education and sense of responsibility would think of expressing in that way and of which there is no indication in section 22 or the other part of section 23. That to my mind would not be choosing between two equally possible and reasonable constructions but adopting a strained construction, unreasonable in effect and out of tune with the policy of the Act that an assessee should make full disclosure of his income. In my opinion the power to call for accounts under section 22 (4) may be exercised by the Income-tax Officer after the assessee has submitted a return, and failure of the assessee to produce his accounts when called for after he has submitted a return may be penalised by arbitrary assessment under section 23 (4); the question referred to us must be answered in the affirmative, and the assessee should pay the costs of the reference Rs. 250.

O. P. No. 186 of 1928.

This reference raises the same question as that decided in O. P. 188/28 and the decision must follow the decision in that case. The reference is not now pressed by the assessee in respect of any other contention. The assessee will pay the costs of this reference, Rs. 150. I think Rs. 150 is quite enough as though it is a different party the case was not argued.

O. P. No. 187 of 1928.

This case raises the same question as that decided in O. P. No. 188/28 and the decision so far must be the same. But in this case it happened that the Income-tax Officer in 1926-27 called for the assessee's accounts both for the year of account and for the preceding year. The accounts of the year of account were produced but not those of the preceding year. On that default the Income-tax Officer proceeded to make his assessment for 1926-27 under section 23 (4) of the Act. The assessee applied for cancellation of the assessment under section 27. The Income-tax Officer refused to reopen the assessment, and in his order refusing to do so he stated that he had wanted the accounts of the preceding year for the purpose of making a revised assessment for 1925-26 under section 34. It is admitted that he had no power at that time to call for the accounts for the earlier year for that purpose as he had issued no notice under section 34. The assessee appealed to the Assistant Commissioner of Income-tax against the refusal of the Income-tax Officer to re-open their assessment for 1926-27. The

(1) 2 I. T. C. 517.

Assistant Commissioner then discovered, and stated in his order, that the Income-tax Officer had required the accounts of the earlier year, not only for the purpose of revising the assessment of 1925-26, but in order to verify the opening balances of the accounts actually produced for the assessment of 1926-27. It is clear that the Income-tax Officer had the power to call for accounts of the earlier year for the purpose of the assessment of 1926-27. The notice which he issued did not disclose for what purpose he wanted these accounts. The fact that he afterwards gave to the assessee a reason which would not justify his action in calling for the earlier accounts did not make his action unjustifiable or illegal; nor did it make the failure of the assessee to produce those accounts an insufficient basis for an arbitrary assessment of their income under section 23 (4) of the Act. The assessment for 1926-27 under section 23 (4) in this case was therefore legal.

The assessees have failed on both the questions raised in this reference. But it will be seen that the second question would never have been raised and the assessees' appeal to the Assistant Commissioner would never have been preferred if the Income-tax Officer had stated in his order on their application under section 27, as the Assistant Commissioner afterwards stated, that he wanted the accounts of the earlier year for the assessment of 1926-27, with which he was then engaged. But he chose to give as his only reason for calling for those accounts a reason which would not justify his action and which the Assistant Commissioner afterwards discovered was not his only reason. It is at least curious that the Assistant Commissioner should afterwards have known that the Income-tax Officer had a good reason for his action which the Income-tax Officer himself did not think of stating in his own order. And, though the reason stated by the Income-tax Officer does not affect the legality of his action or the consequences of it, his statement of his reason in his order was undoubtedly misleading to the assessees and left them under the impression that they had a good case for appeal when they had none. It is much to be regretted that the Income-tax Officer should have misled the assessees and should have given to the proceedings of his department an air of disingenuity. If the only question raised in this reference had been whether the Income-tax Officer had the power to call for the accounts of the earlier year as he did, it would have been proper in the circumstances that the Commissioner of Income-tax should be ordered to pay the costs of the assessees in these proceedings. But, as the assessees have failed on the other question also, which is common to this case and to O. Ps. 186 and 188/28 each party will bear his own costs.

(267) IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Mr. Justice Zafar Ali and Mr. Justice Addison.

[29th November, 1928.]

Khushi Ram—Dukhbanjan Ram Tek Chand

.. Assessees.

v.

The Commissioner of Income-tax, Punjab and N. W.
Frontier Province

.. Referring Officer.

Income-tax Act (XI of 1922), Sec. 3—Pool of Ice Factories—Agreement between proprietors for joint management and division of profit or loss—Assessment as a firm.

Under an agreement dated the 13th January 1925, styled "a partnership of a pool" between the proprietors of three ice factories, it was agreed inter alia

that the manufacture of ice in the factories was to be pooled, the sale to be under the joint management and control of a committee of the three proprietors, the expenses to be debited to joint account and profit or loss to be shared. Subsequently on the 24th May, 1925, the proprietor of a fourth ice factory joined the association agreeing to be governed by the terms of the prior agreement.

HELD, that under the agreement of the 13th January 1925, modified by the agreement of the 24th May, a firm was constituted within the meaning of Sec. 3 of the Income-tax Act.

The Lucknow Ice Association v. Commissioner of Income-tax, United Provinces, 2 I.T.C. 156, Followed.

Case [Civil Reference No. 41 of 1927] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Punjab and N. W. Frontier Province for the opinion of the High Court.

CASE.

In an application dated the 16th May 1927, I was asked by the petitioners to make a reference to the High Court under section 66 (2) of the Income-tax Act. As a result of correspondence, the petitioners in a letter dated the 12th July specified seven questions which they wished referred. By my order dated the 22nd July, I refused to refer four of them, all relating to a single point the disallowance on appeal of a claim for depreciation. The remaining three questions involve a point of law, which arises thus:—

2. By an agreement dated the 13th January 1925, a translation of which is attached and marked Exhibit A,* the proprietors of three ice factories in D. I. Khan formed "a partnership of a pool" for the supply of ice and aerated waters to D. I. Khan and its neighbourhood. The agreement was made because the potential supply of three ice factories was greater than the demand. The main terms of the agreement were as follows:—

- (a) The "partnership" was to continue for four years (condition i).
- (b) Ice was only to be manufactured in one factory at a time, and each factory was to take its turn to manufacture it (condition xi).
- (c) All the ice produced was to be sold at one centre under the control of the joint management of the concern (condition iv).
- (d) For this purpose a committee was to be formed of three proprietors and was to meet once a fortnight or oftener in case of emergency (conditions iv, viii and xix).
- (e) The expenses incurred by the joint management were to be debited to "the partnership accounts" (condition iv).
- (f) Whoever made the ice was to be paid 0-12-0 a maund for whatever was supplied (condition iv).
- (g) Net profit was to be distributed fortnightly according to the shares specified in the agreement (condition v).
- (h) The supply of ice outside D. I. Khan was to be subject to the same conditions. Any one transgressing them would be liable to a penalty (conditions vii & xvi).

* Not printed.

(i) Parties were to share in both losses and profits (condition xii).

(j) Bank accounts were to be in the name of the concern, and all withdrawals were to be signed by all three parties (condition ix).

(k) Each party was entitled to prepare and sell aerated waters, but all sales both wholesale and retail, whether in the bazar or to any individual, were to be done under the partnership agreement, and the proceeds were to be credited to the partnership accounts (condition xiii).

(l) Wholesale prices were to be fixed, and anything obtained over and above the fixed rates was to be credited to the manufacturer, who, moreover, was to be entitled to the proceeds of all retail sales (condition xiv).

3. On the 24th May 1925, the two proprietors of a fourth ice factory were admitted into the association by written agreement, a copy of which is attached and marked Exhibit B.* So far as the supply of ice was concerned, the in-coming partners agreed to be governed by the conditions of the first agreement, which was only modified in so far as was necessary to give them a share in the profits. For the supply of aerated waters, they were not bound by the earlier agreement (condition vii).

4. Both on assessment and on appeal, the concern, as constituted by these two agreements, was held to be an unregistered firm and assessed accordingly. I am now asked to refer the following three questions to the High Court for decision:—

(i) Whether the agreement dated the 13th January 1925, creates a separate firm in the eyes of the law which can justify a separate assessment, or whether it merely creates an agency to sell ice and aerated waters manufactured at any of the factories and divide the proceeds of sales according to certain shares specified therein.

(ii) Whether the Assistant Commissioner was correct in saying that the Income-tax Department was only to look to the words as used in the deed or whether it is not the duty of the Income-tax Department to consider not merely the form but the real nature of the agreement.

(iii) Whether the Income-tax Officer and the Assistant Commissioner have wrongly interpreted the agreement dated the 24th May 1925 as creating a firm, whether it is not correct to hold that this agreement does not show the existence of any firm but merely allows a share of one anna per rupee of profits to another factory in consideration of its ceasing to work.

5. As required by law I now express my opinion on each of these questions. The first question may be more briefly expressed thus:—Was a firm within the meaning of section 3 of the Indian Income-tax Act constituted by the agreement dated the 13th January 1925?

In section 239 of the Indian Contract Act persons who enter into partnership with one another are called collectively a 'firm' and 'partnership' is defined as "the relation which subsists between persons who have agreed to combine their property, labour or skill in some business and to share the profits thereof between them". To constitute a partnership, therefore, the parties concerned must, firstly, combine their property, labour or skill in a business and secondly agree to share the profits of the business between them. In this case the parties concerned agreed to share losses as well as profits, and also to combine

* Not printed.

their labour and skill, for the whole business was to be done under their joint management. The fact that the word 'partnership' (*Sharakat*) occurs 18 times in the agreement is further proof that a partnership existed. The case, in fact, closely resembles that of the *Lucknow Ice Association v. Commissioner of Income-tax, United Provinces*,⁽¹⁾ in which it was held that an association constituted by an agreement very similar to that of the 13th January 1925 was a firm within the meaning of section 3 of the Indian Income-tax Act. I consider, therefore, that this question should be answered in the affirmative.

6. The third question will next be considered and may be expressed thus:—Was the association constituted by the agreement of the 13th January 1925, as modified by the agreement of the 24th May 1925, a firm within the meaning of section 3 of the Income-tax Act?

As explained above, the only effect of the second agreement was to introduce into the association a fourth party the two proprietors of the fourth factory were regarded as single party (condition xi) and to modify the partnership shares accordingly; but the fourth party was to be associated only in the manufacture and sale of ice and not in the manufacture and sale of aerated waters. Thus the second agreement merely enlarged the original association by introducing into it a fourth party in pursuance of the main object of the association, which was the regulation and the control of the sale of ice an object to which the manufacture and sale of aerated waters was entirely subordinate. The answer to this question depends upon the answer to the first. If I am correct in answering that in the affirmative, I would also answer this in the same way, the more so, as the word "partnership" occurs six times in the agreement.

7. There remains the second question. It is very ambiguously expressed and, so far as it can be understood, suggests that the facts of the association did not correspond with the terms of the two agreements. There is, however, nothing on the file to suggest that this was the case, nor is the point mentioned either in the assessment order dated the 10th March 1927 (Exhibit C*), or in the memorandum of appeal dated the 6th April (Exhibit D*), or in the list of the objections given at the beginning of the appellate order dated the 20th April. It does not, therefore, arise and cannot be referred.

Jai Gopal Sethi, for the Assesseees.

Jagan Nath Aggarwal, for the Crown.

JUDGMENT.

This is a reference under section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Income-tax Commissioner of the Punjab and North-West Frontier Province.

Two questions have been referred, namely:—(1) Was a firm within the meaning of section 3 of the Indian Income-tax Act constituted by the agreement dated the 13th January 1925? (2) Was the association constituted by the agreement of the 13th January 1925, as modified by the agreement of the 24th May 1925, a firm within the meaning of section 3 of the Income-tax Act?

In our judgment the Commissioner has correctly answered both questions in the affirmative. We have heard arguments and have been taken very carefully through the provisions of both deeds and the conclusion we have

(1) 2 I. T. C. 156.

* Not printed.

come to is that this case cannot be distinguished from the case *The Lucknow Ice Association v. Commissioner of Income-tax*(1). With that decision we respectfully agree. The answer of the Court, therefore, to both questions asked in the reference is in the affirmative. The assessee shall bear the costs of this reference.

(268) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Sir Murray Coutts Trotter, Kt., Chief Justice, Mrs. Justice Odgers and Mr. Justice Beasley.

[29th November, 1928]

Messrs. Massey & Co., Ltd.

.. Assessee.*

v.

The Commissioner of Income-tax, Madras

.. Referring Officer.

Income-tax Act (XI of 1922), Secs. 10 (2) (vi) & 26—Assessee purchasing a business as going concern—Claim for unabsorbed depreciation allowance of the business taken over—Prior decision of the Commissioner—If res judicata.

The Assessee having purchased the business of E. & Co., Ltd., as a going concern as from 1st Jan. 1924 carried on since that date their own business as well as E. & Co.'s. For the year 1924-1925 the Commissioner held that they were assessable as successors of E. & Co. under Sec. 26 of the Income-tax Act and were entitled to carry forward the depreciation allowance of E. & Co. and in the succeeding years the assessee was allowed to claim E. & Co.'s depreciation allowance. On an assessment for 1927-1928, the assessee's claim under Sec. 10 (2) (vi) of the Act for the depreciation allowance due to E. & Co. and not given effect to during the period of its existence was disallowed.

HELD, that the assessee was entitled to carry forward the depreciation allowance of E. & Co. not given in the years previous to succession by them, such depreciation allowance to be worked out on the original cost to E. & Co. of the assets taken over by the assessee and not at the value at which they took them over.

HELD, further that the prior order of the Commissioner in the assessment proceedings of 1924-1925 would not operate as res judicata so as to prevent that decision from being re-opened in subsequent years.

Case [O. P. 138 of 1928], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

CASE.

I have the honour to refer the following case for the decision of the Hon'ble Judges of the High Court under section 66 (2) of the Indian Income-tax Act XI, 1922.

2. Messrs. Massey & Company (hereinafter referred to as the petitioner Company) object to an assessment made on them for the year commencing the 1st April 1927 on a net income of Rs. 1,19,578.

* (1929) 56 M. L. J. 451 : 29 L. W. 476 : A. I. R. (1929) Mad. 453.

(1) 2 I. T. C. 156.

3. The following facts were proved or admitted:—

(a) The petitioner Company is a Company incorporated under the Indian Companies Act. It owned lands and buildings at Tondiarpet, Madras and there carried on business as Engineers and iron founders and dealers in oil engines, machines and general hardware.

(b) The Madras Engineering Works (hereinafter referred to as the Old Company) was another company incorporated under the Indian Companies Act. It owned lands and buildings at Royapuram and there carried on business almost similar to that carried on by the petitioner Company, with the addition of a department which dealt in printing machines and types.

(c) The petitioner Company carried on a fairly prosperous business whereas the old Company which had come into being mainly for the purpose of taking over a business which was previously being carried on under the style of the Madras Engineering Works (Messrs. Oakes & Co., Ltd., Proprietors) incurred losses in its business from the date of its inception in 1920 with the result that according to its Balance Sheet as on 31—12—1923 it had suffered a net loss of over Rs. 5,00,000.

(d) At the end of 1923 the Directors of the Old Company with a view to eliminate the competition of the petitioner Company acquired a controlling interest in the shares of the petitioner Company and arranged for the amalgamation of the two businesses carried on by the petitioner Company and the old Company respectively.

(e) By a resolution of the Directors dated 5—1—1924 the petitioner Company resolved to purchase the business of the old Company as a going concern as from 1—1—1924 for the consideration following, viz., “Rs. 10 lakhs of Ordinary shares in Massey & Co., Ltd., (petitioner Company) issued as fully paid up to the nominees of the Madras Engineering Works, Ltd., (old Company), Rs. 32,000 and Rs. 3,76,000 being the consideration for the land and buildings respectively; Rs. 3,52,000 being the consideration for the movable plant consisting of Machinery, etc., Rs. 2,00,000, fixtures and fittings, Rs. 70,000, loose tools, Rs. 18,000, Motor cars and launches Rs. 14,000, electrical plant Rs. 50,000 and Rs. 2,40,000 being the consideration for the remaining assets after providing for liabilities and expenses.”

The petitioner Company has since that date been carrying on the business formerly carried on by the two companies—the petitioner company and the old company.

(f) The original cost of the buildings, machinery and plant of the old Company as on 31—12—1923 amounted to Rs. 7,97,453 and on this amount the old Company was entitled if it carried on business to claim an allowance on account of depreciation under section 10 (2) (vi) of the Income-tax Act. In the years of account (Calendar years) 1920, 1921, 1922 and 1923 the business of the old Company had resulted in losses and no allowance on account of depreciation had therefore been given to it. The total amount of depreciation that the old Company was entitled on 1—1—1924 to carry forward under proviso (b) to section 10 (2) (vi) of the Income-tax Act and claim as a deduction against its profits chargeable to income-tax in the following years was Rs. 1,38,784.

(g) The business of the old Company was purchased by the petitioner Company, as stated above, on 1—1—1924. The assessment on the old Company for the year 1924-25 (based on the profits of the Calendar year 1923) was therefore made on the petitioner Company as successor within the meaning

of section 26 of the Income-tax Act though the assessment did not result in any tax becoming payable. In the assessment made on the petitioner Company for the same year, the petitioner Company was further allowed a set off of the trading losses of the old Company against its own taxable profits. A copy of the order of the Commissioner under section 33 dated 24—3—1925 is filed marked Exhibit A.

(h) The business of the petitioner Company resulted in a loss in the Calendar year 1924. No assessment was therefore made on it in the year 1925-26 and it was further permitted to carry forward the depreciation due to it for that year as a deduction against its profits in the following year.

(i) In the year 1925 the petitioner Company made a profit of Rs. 1,39,144 but again no assessment was made on the company in the year 1926-27 as it was found that the deduction on account of depreciation due for that year and that carried forward from the preceding year together exceeded the profits that arose to the Company.

4. During the year 1926 the profits and gains that accrued to the petitioner Company from its business amounted to Rs. 2,08,512. This profit it admitted for the assessment of the year 1927-28 but claimed a sum of Rs. 2,41,924 as a deduction on account of depreciation due to it, as shown under:—

	Rs.	Rs.
(i) Deduction on account of depreciation in respect of the buildings, machinery and plant that belonged to the old Company and to which effect was not given during the period of its existence (see paragraph 2 (f)		1,38,784
(ii) Depreciation due in the assessment of 1925-26 to which effect was not given owing to there being no profits chargeable for that year	81,360	
Depreciation due in the assessment of 1926-27	80,404	
	<u>1,61,764</u>	
Deduct amount allowed in the assessment of 1926-27	<u>1,39,144</u>	22,620
(iii) Deduction on account of depreciation in the assessment of 1927-28		<u>80,520</u>
		<u>2,41,924</u>

The depreciation worked by the petitioner Company for the years 1925-26, 1926-27 and 1927-28 (years of account 1924, 1925 and 1926) was based, in respect of the buildings, machinery and plant taken over from the old Company on their *original cost to the old company* and not on their *original cost to the assessee*, i.e., the petitioner company.

On the basis of the figures contained in the preceding paragraph the petitioner Company contended that no assessment should be made on it for the year

1927-28 and further claimed that it should be permitted to carry forward a sum of Rs. 33,412 being the allowance for depreciation which could not be given effect to in the assessment of that year.

5. The Income-tax Officer held,

(i) that the depreciation due to the old Company was personal, and that the petitioner Company though it was liable as successor to the business of the old Company to pay the tax due by the old Company in the year of succession was not entitled to any deduction on account of depreciation which the old Company could have claimed had it been in existence, and

(ii) that the depreciation due to the petitioner Company on account of buildings, machinery, plant, etc., taken over from the old Company should be worked out on the basis of the cost to the assessee, i.e., to the petitioner Company and not on their original cost to its predecessor; such cost was ascertainable from the terms of the Resolution dated 5—1—1924—see paragraph 2 (e) above. He accordingly worked out the depreciation due to the petitioner Company as under:—

	Rs.
Depreciation for the year 1924 not given effect to in the assessment of the year 1925-26. ..	75,928
Depreciation for the year 1925 ..	75,263
	<hr/> 1,51,191
Depreciation allowed against the profits of the year 1925 in the assessment of 1926-27 ..	1,39,144
	<hr/> 12,047
Balance to be carried forward ..	12,047
Depreciation for the year 1926 to be allowed in the assessment of 1927-28 ..	76,887
	<hr/> 88,934
Total depreciation due. ..	<hr/> 88,934

Deducting this amount from the profits of the petitioner Company for the year 1926, i.e., Rs. 2,08,512 the Income-tax Officer assessed the petitioner Company on the balance of Rs. 1,19,578.

6. The petitioner Company appealed against the assessment and contended *inter alia*: (a) that it should be allowed the depreciation which was due to the old Company and to which no effect could be given during the period of its existence, and (b) that the depreciation on the buildings, machinery and plant taken over by it from the old Company should be worked out on the basis of their original cost to the old Company and not on the value at which they were taken over by it. The Assistant Commissioner agreed with the conclusions of the Income-tax Officer and dismissed the appeal. His order is filed marked Exhibit B.*

7. The petitioner requires me to state a case and refer for the decision of the High Court the following questions of law that arise out of the order of the Assistant Commissioner under section 31:—

(1) Whether Messrs. Massey and Company Limited who succeeded to the business of the Madras Engineering Works Limited are entitled to carry

forward for the purposes of assessment depreciation to which full effect could not be given in the years previous to the succession by Massey and Company Limited.

(2) Whether Messrs. Massey and Company Limited can be allowed to calculate depreciation on assets taken over from the Madras Engineering Works Limited on the original cost of those assets to the latter, or at the value at which they were taken over by Messrs. Massey and Company Limited.

(3) Does the order dated 24—3—1925 under section 33 of the Income-tax Act operate as *Res judicata* so as to prevent the decision from being reopened in assessments made in years subsequent.

My opinion on these questions is as follows:—

Question (1). Under section 10, sub-section (2), clause, (vi) of the Income-tax Act, in computing the profits and gains of his business an assessee is entitled to an allowance on account of depreciation in respect of “buildings, machinery, plant or furniture being his property.” The depreciation now claimed by the petitioner Company is what was due to the old Company before the succession. The buildings, etc., of which the old Company were then the owners were not therefore used in the business of the petitioner-company, nor were they the property of the petitioner-company within the meaning of clause (vi) to sub-section (2) of section 10, during the years for which depreciation is now claimed. In my opinion the deduction on account of depreciation is personal to the persons who carry on the business and as the petitioner-company did not carry on the business of the old Company during the years for which it now claims depreciation its present claim is inadmissible.

Question (2). Section 10, sub-section (2) clause (vi) of the Income-tax Act on which the petitioner-company bases its claim enacts that an allowance for depreciation in respect of buildings, machinery, etc., should be made in a sum equivalent to such percentage of the *original cost to the assessee* as may be prescribed. The assessee in this case (and the person who claims the allowance on account of depreciation) is the petitioner-company and the original cost to it of the buildings, machinery, etc., taken from the old Company is the cost at which it authorised its Directors to purchase them from the old Company and at which they are valued in its accounts. In my opinion the petitioner-company is entitled to claim depreciation only on the cost of those assets which it had paid and not that at which they were purchased by the old company.

Question (3). *Res Judicata* presupposes that there are two opposing parties, that there is a definite issue between them, that there is a tribunal competent to decide the issue and that within its competence the tribunal has done so. In a proceeding before an Income-tax Officer none of these various elements which are necessary for the application of the principle of *res judicata* are to be found and in my opinion the doctrine cannot be applied to an Income-tax proceedings.

EXHIBIT A.

Copy of Proceedings of the Commissioner of Income-tax, Madras No. 420/25, dated 24th March 1925.

Reference to High Court—Application for—Massey & Co., Ltd., Madras-1924-25.

On the facts now brought out, I consider that there was a succession within the meaning of section 26. The assessment on Messrs. Massey & Co., for 1924-25 is accordingly cancelled. The tax paid will be refunded. Messrs.

Massey & Co., are entitled to carry forward the depreciation allowances not given in the past to the Madras Engineering Works. The exact figures to be carried forward will be settled by the Income-tax Officer.

(Sd.) D. N. STRATHIE,

Commissioner.

Nugent Grant, for the Assesseees.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

THE CHIEF JUSTICE:—The only question I propose to ask myself in this case is whether or no there is anything to distinguish it from the Scottish case of the *Scottish Shire Line Limited v. Letham*(1). That was a very strong Court consisting of the Lord Justice Clerk, Lord Dundas, Lord Salveson and Lord Guthrie. Therefore I should feel myself constrained and do feel myself constrained to follow those eminent Judges unless it can be shown that there is either something on the facts to distinguish this case from that, or that there is a material variation in the language respectively of the Indian and the corresponding English section. I say advisedly material because Indian draftsmen for some reason are always making little changes of language which do not mean anything at all vital to the true construction of the Act. With regard to the facts I am unable to see that anybody could argue that there is the slightest distinction between the relation of Massey & Co., Ltd., here to the Madras Engineering Works and the relation between the Scottish Shrine Line, Ltd., and the Elderslie Steamship Co., Ltd., of the Scottish case.

The only other question is, can we find any difference between the language of the Indian Act with which we are concerned and the language of the Finance Act, 1907, on which the Scottish case was a decision? I am not going to read the two sections at length. It is sufficient to say that I have scrutinised them very carefully with the aid of counsel and that I am quite clearly of opinion that there is no material difference in the language and that, whatever was intended to be effected, the aim and object of the Indian Act is absolutely the same as that of the English Act. I am therefore of opinion that this case is quite indistinguishable from the Scottish case and that the reasoning of the learned Judges there apply directly to our case. One consideration to which I am referring is put forward in Lord Guthrie's judgment at page 100. What he says is this:—"It appears to me that the argument of the Surveyor of Taxes has neither probability nor equity in its favour, because he proposes to treat the appellant company as identical with or as the successors of the Elderslie Steamship Co., Ltd., (called the old company in the case) for one revenue purpose, and neither as identical with nor as the successors of the old company for another and not remotely related revenue purpose."

Similar passages are to be found in the other two learned Judges' judgments. That to my mind is precisely what the Income-tax Officer is trying to do in this case and for the reasons given by the Scottish Court I decline to accede to that course being adopted. The answer therefore to the first question is in the affirmative; the answer to the second is that the calculation must be made on the original cost to the Madras Engineering Works and not on the value at which the buildings, machinery, etc., were taken over by Massey & Co. The answer to the third is in the negative.

The Crown will pay Rs. 250 costs to the assessee and refund Rs. 100.
ODGERS J.:—I agree.

BEASLEY J.:—I agree.

(269) IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Mr. Justice Zafar Ali and Mr. Justice Addison.

[29th November, 1928.]

Khan Muhammad Yakub Khan and Khan Muhammad Aslam
Khan .. Assesseees.

v.

The Commissioner of Income-tax, Punjab and N. W.
Frontier Province. .. Referring Officer.

Income-tax Act (XI of 1922), Secs. 2 (1), 4 (3) (viii) and 10—Possessory mortgage of lands—Mortgagee to receive lease amounts from lessee in possession—Subsequent sale of mortgaged lands to mortgagee—Purchase money adjusted in part towards mortgage claims—Claim of exemption as agricultural income—Amounts, when received.

Under a possessory mortgage of lands dated the 27th November 1916, the mortgagee was to receive the annual lease amounts from the lessees already in possession and in default of payment by the lessees, the amounts were to be added to the mortgage amount and to be recovered from the mortgagor in lump sum at the time of redemption. On the 4th May 1923, the mortgagor executed another deed charging the mortgaged lands with the payment of Rs. 30,000 being the lease amounts from May 1917 to May 1923 not paid by the lessees. On the 24th February 1925, the mortgaged lands were sold to the mortgagee for 2 lakhs paid in cash after deducting Rs. 30,000 due under the deed of the 4th May 1923, Rs. 7,500 the lease amount from May 1923 to February 1925 and Rs. 40,000 the principal mortgage amount. On an assessment of this sum of Rs. 37,500 as interest income of the mortgagee doing money lending business received during the account year 1924-1925, the mortgagee claimed exemption from assessment as agricultural income and further contended that the sum of Rs. 30,000 was not received on the date of the sale but earlier when the deed of 4th May 1923 was executed.

HELD, that the mortgagee being entitled only to a fixed sum and having no concern in the produce of the land or the possession thereof, the sums received could not be said to be income from land within the meaning of Sec. 2 (1) of the Income-tax Act and that the sum of Rs. 30,000 was received by the mortgagee only when the same was deducted from the purchase money and not earlier when it was secured as a charge.

Case [Reference Case No. 4 of 1928] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Punjab and N. W. Frontier Province for the opinion of the High Court.

CASE

As requested by the petitioners I hereby refer under section 66 (2) of the Income-tax Act, 1922, for the decision of the Hon'ble Judges of the High

Court the following two questions of law arising out of an order passed by the Assistant Commissioner of Income-tax, Northern and Frontier Division, under section 31.

(a) If a person who lends a sum of money on the security of land of which he takes a mortgage with possession on the condition that he will receive an annual payment during the term of the mortgage, does not receive the payment stipulated upon, but obtains a further mortgage deed for the arrears due and finally purchases the land, receives payment by way of deduction from the sale money agreed upon of the original sum loaned plus the annual recurring payment due, can the sum received in excess of the original loan be regarded as interest and not as "agricultural income" within the meaning of section 2 (1) of the Act?

(b) Can the entire sum received over and above the original sum advanced be said to have been received in the year when the sale money was paid, or should the sum included in the second mortgage deed be said to have been received when the second mortgage deed was executed?

2. The facts of the case are that after the original assessment for the year 1925-26 had been made on an income of Rs. 18,537, it came to the notice of the Income-tax Officer of Peshawar that the petitioners, who do business in money-lending, had received during the year 1924-25 (the "previous year" for the purposes of the assessment for 1925-26) a sum of Rs. 37,500 as interest from one Jaffar Khan, whose lands were mortgaged to the petitioners. As a result of proceedings under section 34 of the Income-tax Act, the sum of Rs. 37,500 was added to the original assessment, and a further demand of Rs. 4,384|9 on account of income-tax and Rs. 377|5 on account of super-tax was made. The petitioners appealed against this additional assessment, but the appeal was unsuccessful. It is necessary to relate how the sum of Rs. 37,500 came into the possession of the petitioners.

On the 27th November 1916 Jaffar Khan and Sher Dil Khan, proprietors of village Saidabad leased the village to one Nawab Khan for 16 years at an annual sum of Rs. 10,000. On the 12th May 1917, Jaffar Khan, one of the proprietors mortgaged with possession to one Khan Sher Ali Khan, the father of the petitioners, his half share of the village for ten years for Rs. 40,000. According to the mortgage deed, a translation of which is attached as Exhibit A, Jaffar's share of the annual lease money, viz., Rs. 5,000, was to be received by the mortgagee, and in case the lessee made default the amount was to be recovered from Jaffar Khan and his heirs and not from the lessee, or the amount in default was to be added to the mortgage money and to be paid at the time of redemption of the land in a lump sum. It was further agreed that the mortgagor would have no right to redeem the land nor the mortgagee any right to claim the mortgage money within the period of ten years. Further the deed stipulates that if the lease terminates or ceases during the period of mortgage, the mortgagee will get possession of the land. No payment of lease money having been made to the mortgagee, Jaffar Khan executed a further deed, on 4—5—1923 (Exhibit B) in favour of the former mortgagee's sons (the petitioners in the present case), the father having died, for Rs. 30,000 on account of lease money for six years from May 1917 to May 1923. This sum was to be an additional encumbrance on the land already mortgaged. This additional charge did not affect the annual lease money which had to be paid as before. The lease was cancelled on the 3rd July 1923, and the possession of the lands restored to the landlords. On the 24th February 1925, Jaffar Khan sold his share of the land to the mortgagee (petitioners) for two lakhs (Exhibit C).

The balance of the sale price was paid in cash after deducting Rs. 30,000 due on the mortgage deed executed on the 4th May 1923, Rs. 7,500 on account of lease money from May 1923 to February 1925, and the Rs. 40,000 for which the land was originally mortgaged. As a result of this transaction between Jaffar Khan and the petitioner the latter received a sum of Rs. 37,500 by deduction of the sale money agreed upon over and above the Rs. 40,000 originally loaned to Jaffar Khan. He claimed that this was agricultural income within the meaning of section 2 (1) and, therefore, exempt from income-tax under section 4 (3) (viii). The assessing officer held that it was interest on the sum advanced on the mortgage of the lands and that there was a simple mortgage, and as the assessee does business in money lending, assessed it under section 10 as it represented interest at $12\frac{1}{2}$ per cent p. a. on the original sum advanced.

3. Now as regards the first point, agricultural income, as defined in section 2 (1) (a) of the Act means "any rent or revenue derived from land which is used for agricultural purposes and is either assessed to land revenue in British India or subject to a local rate assessed and collected by officers of Government as such". To secure an exemption under this definition it must be shown (1) that the income is derived from land, (2) that the land from which it is derived is used for agricultural purposes, and (3) that it is either assessed to land revenue or subject to a local rate assessed and collected by officers of Government as such. Now, in all the circumstances of the case, can this sum of Rs. 37,500 be said to have been received from rent or revenue derived from land which is used for agricultural purposes, or is it a receipt from interest on a simple mortgage of land? It will be recalled that the entire village was leased for sixteen years, and six months later, one of the proprietors mortgaged his share with possession for ten years. While the mortgage lasted, the lease was cancelled and the lands reverted to the possession of the original owners and about two years later the mortgagor's share was sold to the petitioners, who were allowed a deduction of the original mortgage money Rs. 40,000 plus Rs. 37,500 on account of the payment due under the terms of the mortgage deed (Exhibit B) executed on the 4th May 1923. The petitioners take their stand on what is said at p. 82 of the Law of Income-tax by V. S. Sundaram in the para headed 'Land Leased or Mortgaged'. This para reads as follows: "The land need not be cultivated by the owner himself. It can be leased in which case it would still be income from agriculture both to the lessor and to the lessee. If the land is mortgaged, it will be agricultural income in the hands of the mortgagee if it is a usufructuary mortgage, but not if it is a simple mortgage. In the latter case, of course, the owner would receive the agricultural income himself while the mortgagee would be merely in receipt of income from money lending, which would not be affected in any way merely because he had a right to attach the property in case the debt was not paid. Where there are intermediary lessees or tenure holders whatever the nature of interest and whatever the local tenure, zamindari, ryotwary or anything else, the income of all these holders and lessees is clearly agricultural".

According to this if the land is mortgaged it will be agricultural income in the hands of the mortgagee if it is a usufructuary mortgage, but not if it is a simple mortgage. The terms of the mortgage deed, no doubt, show that the mortgage was with possession, but the fact that the land was under lease when the mortgage was entered into, that on the cancellation of the lease it reverted not to the possession of the petitioners but to the former owners, shows that there was no intention of entering into possession, but that the sole object was to secure re-payment of the sum advanced along with the interest

accruing on that sum. In a decision given by the Judicial Commissioner of Peshawar in the Civil appeal of *Gopi Chand S/o Dunni Chand Utmanzai v. Muhammad Umar and others*, it has been held that in cases where land is mortgaged with possession and the mortgagee gives a lease of the land to the mortgagor on payment of a certain sum, there is no intention of parting with the possession but the transaction is to be deemed one of simple mortgage and the amount so received by the mortgagee is really interest. A perusal of the judgment above cited shows that it has been held in the Judicial Commissioner's Court at Peshawar that notwithstanding that the mortgage deed shows in so many words that the mortgage was with possession, it is permissible to examine the acts and conduct of the parties to ascertain the real intention. This dictum has been reaffirmed in the decision by the Madras High Court in *Commissioner of Income-tax, Madras v. Subramanya Sastrigal*(1). All the circumstances of the case show positively that this was a simple mortgage and that the payment represented was interest on the money advanced under a mortgage. The petitioners, it may be noted, have been earning interest from money lending in past years. Accordingly I submit that the answer to the first point should be that the income can be regarded as interest and not as agricultural income.

4. Turning now to the second point, viz., whether the entire sum can be said to have been received in 1924-25, when the payment of the sale money was made, or whether Rs. 30,000 was received by the petitioners in 1923-24, when the second mortgage deed was executed. The petitioners contend that the latter sum was received when a fresh deed was executed in their favour on the 4th May 1923 (Ex. B) when it was made a charge on the land and was in the nature of mortgage money and that if actual receipt in cash is to be the criterion it has not been received. In *Gresham Life Assurance Society vrs. Bishop*, quoted in the case of *Pandurang v. Commissioner of Income-tax, C. P.*(2) decided by the Court of the Judicial Commissioner at Nagpur, it was held that a sum of money may be received in more ways than one, e.g., by the transfer of a coin or negotiable instrument or other document which represents and produces coin and is treated as such by business men. Here we have a case of a person doing business in money lending who advanced a sum of money on a mortgage of land on the condition that payment would be made at a specified rate per annum and that payment works out to the equivalent of 12½ per cent. per annum on the sum advanced. The payment is not made and the accrued sum due for six years, viz., Rs. 30,000, is included in a fresh mortgage deed executed on the 4th May 1923. When subsequently two years later the sale of the land to the mortgagee took place payment was made by deduction of the original mortgage money plus the accrued payment of Rs. 37,000, due on it. There was no receipt at the time the mortgage deed was executed and the money could not have been deemed to have been received then as a mortgage is only an additional security for the loan. The money could only be deemed to have been received when the property was sold to the mortgagee and the amount credited in the sale deed. The fact that credit was afforded to the assessee for the sum of Rs. 37,000 when the sale took place on the 24th February 1925, is, in my opinion, sufficient to establish the receipt of the income and the date of such receipt. The answer to the second question should, in my opinion, be that the entire sum of Rs. 37,000 was received in the accounting period 1924-25, when the sale price was paid.

A copy of this draft was sent to the petitioner in accordance with rule 11 of the Rules framed by the High Court. The petitioner has no amendments

(1) 2 I.T.C. 152.

(2) 2 I. T. C. 69.

to make but asks that a copy of the grounds of his appeal and of the application under section 66 (2) should be attached. Copies are accordingly attached as Exhibits D.* and E.*

EXHIBIT A

Translation of the 1st Mortgage deed dated 12th May 1917.

Stamp Rs. 400.

I Jaffar Khan S/o Bahram Khan, Caste Afghan Khankhel, resident of village Hoti, Tehsil Mardan, District Peshawar, do hereby, in accordance with the terms of this deed, mortgage with possession for a term of 10 years my share of 9055 Kanals 17½ marlas of land out of 18111 Kanals 15 Marlas entered as Khasra No. 1 to 571, Khata No. 1-2|120 in the jamabandi of village Saidabad, for the year 1914-15, for Rs. 40,000 (half of which is 20,000) in favour of Sher Ali Khan S/o Sarbaland Khan, caste Afghan Khankhel, of Hoti. Possession of the proprietary rights has been given to him. But as the whole of the village has already been leased under a registered deed dated the 28th November 1916 by me and my brother to one Nawab Khan for a term of 16 years at an annual rent of Rs. 10,000 the mortgagee will, therefore, receive half of the yearly rent of my share from the lessee according to the term of the lease. In case the lessee fails to pay the annual rent, the mortgagees shall not sue the lessee or his heirs, but I and my descendants and heirs shall be responsible for the payment of the annual rent and shall get a regular receipt for the same. In case of default such items will be added to the mortgage money and will be paid at the time of the redemption of the land in a lump sum. Hence it is extremely necessary for keeping the accounts clear that a regular receipt should be obtained for each payment, in absence of which no payment shall be admitted. I shall have no right to redeem the land nor the mortgagee shall have a right to claim the mortgage money within the period of mortgage. After the expiry of the term of this deed the land shall be redeemed by repaying the full mortgage money, otherwise the mortgage shall continue. If during the period of this mortgage the lease terminates or ceases, the mortgagee shall get possession of the land. I hold myself responsible for the correctness of the transaction. The whole of the mortgage money will be received before the Sub Registrar at the time of the registration of the deed. Mohammad Yakub Khan, the eldest son of the mortgagee is present on behalf of his father (the mortgagee) for the completion of this deed. The term of mortgage begins from today's date but the rent for the current Rabi will be taken by me and thereafter it will go to the mortgagee. Henceforth I execute this deed so that it may serve as a documentary proof.

Written on 12—5—1917 and signed by all concerned.

EXHIBIT B

Translation of the 2nd Mortgage deed dated 4th May 1923.

Stamp worth Rs. 450.

I am Jaffar Khan S/o Bahram Khan, caste Afghan Khankhel, of Hoti District Peshawar. I had, under a registered mortgage deed dated 12—5—1917, mortgaged with possession my 9055 Kanals 17½ marlas of land being the one half share of 18111 Kanals 15 marlas situated in village Saidabad and entered as

Khasra No. 1 to 571 Khata No. 1-2|1-120 in the jamabandi of 1914-15, for Rs. 40,000 (half of which is 20,000) for ten years in favour of Sher Ali Khan deceased S/o Sarbaland Khan deceased of Hoti. The mortgagee was authorized thereby to realise the annual rent of Rs. 5,000 from Nawab Khan lessee to whom the land had already been given on lease for 16 years by a lease deed dated the 28th November 1916 and in case of default I had held myself and my successors responsible for the payment of the rent and to get a receipt for the same or to add the amount in default to the mortgage money. As the rent for 6 years from Kharif 1917 to Rabi 1923 amounting to Rs. 30,000 stands unpaid both by myself and the lessee, I do hereby quite save and sound, assuming my responsibility of payment of Rs. 30,000 to the mortgagee (who has since died and his sons Mohammad Yakub Khan and Mohammad Aslam Khan are his heirs) add its encumbrance on the land mortgaged i.e., this sum of Rs. 30,000 is added to the previous consideration money which shall be repaid at the time of the redemption. Hence I execute this further mortgage deed in favour of Mohammad Yakub Khan and Mohammad Aslam Khan sons of the deceased mortgagee to stand as a documentary proof.

Written on 4—5—1923 and signed by all concerned.

EXHIBIT C

Translation of the sale deed dated 24th February 1925.

I Jaffar Khan S/o Bahram Khan, Afghan Khankhel, resident of Hoti, Tehsil Mardan, District Peshawar, do hereby sell for Rs. 2 lacs (half of which is Rs. 1 lac) 9055 Kanals 17½ Marlas of land of my one-half share in 18111 Kanals-15 Marlas, Khasra Nos. 1 to 571 with all the proprietary rights in the village habitation and common lands situated inside and outside the village. This land is already mortgaged with possession to Mohammad Yakub Khan and Mohammad Aslam Khan S/o Sher Ali Khan deceased for Rs. 77,750 as detailed below:—

Under a mortgage deed dated 12—5—17 for Rs. 40,000

Under a further mortgage deed dated 4—5—23 for Rs. 30,000.

For a further encumbrance of Rs. 7,750 on account of rent of 3 harvests from Kharif 1923 to Kharif 1924. The sale money has been received by setting off Rs. 77,500 on account of the previous mortgages noted above and rupees one lac and twenty two and a half thousand to be received in cash before the Sub-Registrar. The possession of the land has been made over to the vendees who will in future be the proprietors of ½ of the village Saidabad like myself. I cease to be the owner of any portion of the land in that village. I had entered into an agreement with the sons of Nawab Khan of Gulabad for the mortgage and sale of 2400 Kanals of irrigated lands out of the land sold but the agreement is without consideration. I therefore undertake the responsibility of any defect in the ownership and in case the aforesaid area is released from the possession of the vendees, I bind myself to give them an area of equal status and value out of my lands Khata Khewat No. 2 situated in village Karangh. But the vendees shall secure possession of the Karangh land after my death. I shall retain its possession during my life-time and shall myself get the income thereof without sharing it with the vendees. Whether the area, for which an agreement was entered into with the sons of Nawab Khan of Gulabad, remains under the possession of the vendees or not, my brother Sher Dil Khan with whom no partition concerning Saidabad has been effected so far, shall in either case, have a right to have all

kinds of lands (waste or superior) partitioned, or he may keep for himself according to his choice an area equal in value and status in lieu to other.

Written on 24—2—1925 and signed by all concerned.

Zafar Ullah Khan, for the Assessee.

Jagan Nath Aggarwal, for the Crown.

JUDGMENT

The facts relevant to this reference under section 66 (2) of the Income-tax Act of 1922 may be summarized thus:

One Jaffar Khan mortgaged for Rs. 40,000 his half share in a village to Sher Ali Khan who practised money-lending. Though the mortgage was described to be with possession, the land was already in the possession of a lessee, and he was liable to pay as lease money Rs. 5,000, annually to Jaffar Khan on account of his half share in the village. Under the mortgage Sher Ali Khan became entitled to receive this lease money, but it was stipulated that if the lessee should fail to pay the money it would be recovered by the mortgagee from Jaffar Khan and not from the lessee, and that the amount in default would be added to the mortgage money to be paid at the time of redemption in a lump sum. No payment having been made for six years, the sum of Rs. 30,000 due as lease money was made a charge on the land by a deed executed by Jaffar Khan on the 4th May 1923, in favour of the two sons of Sher Ali Khan who had died before that date. On the 24th February, 1925, Jaffar Khan sold the property to the sons of Sher Ali Khan for two lacs and, deducting the original mortgage money (Rs. 40,000), and the additional mortgage money (Rs. 30,000) and the lease money for the subsequent period upto 24th February 1925, (Rs. 7,500), he received the balance in cash.

The questions referred to briefly are:—(1) Whether the fixed annual amount of Rs. 5,000 which the mortgagee was entitled to receive was income from the agricultural land mortgaged, and not interest? (2) Whether the amount of Rs. 30,000 was received on the 4th May, 1923, and not on the date of the sale.

The Income-tax authorities have decided that the fixed sum which the mortgagee was entitled to receive annually was really interest at the rate of $12\frac{1}{2}$ per cent. per annum on the money advanced and that the sum of Rs. 30,000 had not actually been received by the mortgagees until they purchased the land. The mortgagees contest both these conclusions but both appear to us to be correct.

The mortgage, though described as with possession, was in fact a simple mortgage and, from its terms, it is clear that the mortgagee was only entitled to a fixed sum in consideration for the money lent, and had otherwise no concern in the produce of the land or with the possession thereof. This fixed sum, therefore could not be said to be income from the land. The lease money or income from the land was as a matter of fact received by the lessor himself.

As regards the mortgage for the additional sum of Rs. 30,000, it is clear that the mortgagee did not actually receive that amount on the 4th May 1923, though he secured it as a charge on the property mortgaged. He actually realised this amount when he purchased the land and deducted it from the purchase money.

We, therefore, agree with the conclusions arrived at by the learned Commissioner and answer the questions accordingly.

(270) IN THE COURT OF THE JUDICIAL COMMISSIONER, NAGPUR.

Before Mr. Kinkhede, Additional Judicial Commissioner.

[30th November, 1928.]

Gulabrai Govindrai Firm

... Assessee.

v.

The Commissioner of Income-tax, Central Provinces & Berar.

Income-tax Act (XI of 1922), Sec. 66—Specific Relief Act (I of 1877), Sec. 45—Refund of tax, disallowance of—Unsuccessful application to Commissioner for revision and reference—Application for mandamus—Jurisdiction of Court.

An assessee claiming that a certain sum of money was provisionally treated as income and assessed to income-tax pending an adjudication of the Civil Court applied for a refund of tax on that amount. The refund was refused but the assessee was directed to claim the amount against the profits of the following year. After unsuccessfully moving for review and revision by the Commissioner as well as a reference under Sec. 66 (1) of the Income-tax Act, an application was made under Sec. 45 of the Specific Relief Act to direct the Commissioner to state a case under Sec. 66 (1). On a preliminary objection,

HELD, that the Court had no jurisdiction to compel the Commissioner to make the reference.

Application [Misc. Judicial Case No. 16-B of 1928] under Sec. 45 of the Specific Relief Act (I of 1877) for compelling the Commissioner of Income-tax, Central Provinces and Berar, to state a case under Sec. 66 (1) of the Income-tax Act (XI of 1922).

The facts of the case are as follows:—

1. The applicant firm who are businessmen, had to receive from one Debidatta Premasukdas of Cawnpore certain amounts under a decree of the 2nd Additional District Judge, Akola in Civil Suit No. 17 of 1923 and also under an indenture by which the said Debidatta Premasukhdas had bound himself to pay Rs. 6,000 per year to the applicant firm. On or about 16th February 1925, the said Debidatta, who had come to Akola, paid a sum of Rs. 10,000 to the applicant firm. The applicant by an entry in their account books appropriated this amount towards the debt due under the indenture believed to be towards and in lieu of certain commission which the applicants were entitled to receive. So if the amount was in respect of this indenture it would be "income" under the Act and assessable; while if the amount was paid towards the decree it would be only recovery of debt and not assessable. Later on when the applicants tried to execute the decree in C.S., No. 17 of 1923 the J. D. in the case i.e., Debidatta pleaded that the amount of Rs. 10,000 had been paid in part satisfaction of the decree and claimed credit for the same.

2. As the applicant had appropriated the sum towards commission, he showed it as income in his return for the year ending Diwali 1924 A.D. This can be verified by reference to his case No. 438 of 1925-1926. It so happened however, that when his return was being checked the dispute was pending in the Civil Court and the applicant brought the fact of the dispute to the notice of the Assistant Commissioner who remarked in his order to the following effect. "I have treated it (the amount of Rs. 10,000) income. In case the decision of the High Court is adverse to the assessee he will be free to claim it when the deci-

sion is given''. It needs hardly be said that the words 'free to claim it'' in the above context mean that the applicant will be able to claim *a refund of the amount recovered from him in respect of the amount of Rs. 10,000 as tax*. Later on the High Court held in First Appeal No. 82-B of 1925 decided on 21-9-1926 that the said amount of Rs. 10,000 had been paid towards the decree and not towards the commission amount. This decision of the High Court has become final as no appeal was permitted to be filed to the Privy Council. Thus under the wording of the order quoted above the applicant became entitled to a refund of the amount as tax on the amount which comes to Rs. 937-8-0.

3. The applicant thereupon applied to the office for a refund of this amount; the Assistant Commissioner however passed an order on the application (date not known) to the effect that the assessee should claim it against profits of the year following. This order was communicated to the applicant some time after 5th April 1927 by the Income-tax Officer, Akola. As this order was no order for refund at all the applicant again moved the Assistant Commissioner to reconsider the application and prayed for refund. This application was also rejected on 30-4-27 and prior order was quoted to him.

4. Thereafter the applicant applied to this Court (The Court of the Income-tax Commissioner) for a review of the said order but the review was not granted and he was informed on or about 8th July 1927, that the same was rejected. Income-tax Revision case No. 53 of 1927-28 decided on 4-7-27.

5. The applicant thereupon moved the learned Commissioner of Income-tax to refer the questions of law involved to this Hon'ble Court under section 66 (1) of the Income-tax Act, 1922. This application was disallowed on 5-9-1927 by observations embodied in an order of which a certified copy is filed herewith:

The applicant now approaches this Hon'ble Court in its extraordinary jurisdiction exerciseable under section 45 of the Specific Relief Act with the request that the Income-tax Commissioner be required now to state a case and refer points of opinion on the following questions of law, viz:--

(i) Whether the Income-tax Department is not liable to make good its promise of refunding the amount of the tax that came to be levied on the provisional understanding that the amount of Rs. 10,000 credited by the assessee on or about 16-2-25 and in respect of which the Assistant Commissioner had recorded an order to the following effect viz:—"I have treated it (the amount of Rs. 10,000), income. In case the decision of the High Court is adverse to the assessee, he will be free to claim it when the decision is given".

(ii) Was not the assessment as made by the Assistant Commissioner a provisional assessment liable to be modified not only on equitable ground but also because of an express understanding between the Crown and the assessee.

(iii) Has the assessment of the year been finally made. If not is not the Income-tax Department bound to proceed to make a final assessment in view of the decision of this court in First Appeal No. 82-B of 1925, dated 21-9-26 and the promise of the Income-tax Officer to recalculate the assessable income on deducting from the provisional income figure the amount of Rs. 10,000.

(iv) Is it not *ultra vires* or inequitable on the part of the Income-tax Department to reduce the really assessable income of the year 1926-27 by a figure of Rs. 10,000 just because in the calculation of the assessable income in

the year 1925-26 the figure was unwarrantedly rushed up by a sum of Rs. 10,000.

(v) Is the Income-tax Department right in holding that because of the assessee's accounts being kept on the cash system, the High Court's decision in First Appeal No. 82-B of 1925, dated 21-9-1926, and the undertaking or promise of the Assistant Commissioner was not under the circumstances sufficient to require the Crown to again calculate the income amount by reducing the already assessed figure by Rs. 10,000.

(vi) In view of the special procedure of tentative assessment was not the Income-tax Department bound to consider the question of recalculating the assessable income in the case No. 438 of 1925-26, dated 27-1-1926, irrespective of the consideration as to the manner in which the assessee maintains his account books and without expecting him to show the said credit of Rs. 10,000 in February 1925, wiped out by an adjustment entry 21-9-1926, the date of the decision in First Appeal No. 82-B of 1925, probably in account year of 1922-23 Sambat, as observed by the Commissioner.

PRAYER:—In the interest of justice and in vindication of the principle of restraining the Crown from resorting to any procedure of levying an undue tax or retaining any sum which cannot be due to it under law in a given year, this Hon'ble Court may call on the Commissioner to state the assessee's case and refer the above mentioned points of law for its opinion so as to lead the Commissioner to make a final or proper assessment for the year 1925-26.

W. B. Pendharkar, for the assessee.

D. N. Chowdhary, for the Crown.

JUDGMENT.

I think the preliminary objection of the Advocate for the Commissioner of Income-tax must prevail. On the analogy of the ruling in *Thrikamji Jiwan Das v. Commissioner of Income-tax*(1) I hold that this Court has no power to compel reference in the circumstances that exist in this case. The application is therefore rejected. Costs on the party incurring them.

(271) IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Mr. Justice Tek Chand and Mr. Justice Aga Haidar.

[4th December, 1928.]

Messrs. Manohar Lal Dev Karandas

.. Assessee.*

v.

The Commissioner of Income-tax, Punjab and N. W. Frontier Province.

Income-tax Act (XI of 1922), Secs. 23 (4) and 34—Assessment under Sec. 23 (4)—Re-assessment by succeeding Officer under Sec. 34, legality of.

A succeeding Income-tax Officer is competent to re-assess under Sec. 34 of the Income-tax Act an assessment made by his predecessor under Sec. 23 (4) of the Act.

(1) 1 I. T.C. 406.

* A. I. R. (1929) Lah. 178.

Bulaki Shah v. Crown, 1. T. C. 256; *Sundaresa Aiyer v. The Commissioner of Income-tax, Madras*, 2 I T. C. 173. Followed.

Application [Case No. 180 of 1928] under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) for an order directing the Commissioner of Income-tax, Punjab and N. W. Frontier Province to state a case for the opinion of the Court.

Raj Kishan and Hem Raj Mahajan, for the Assesseees.

Jagan Nath Aggarwal, for the Crown.

JUDGMENT.

This is an application under section 66 (3) of the Indian Income-tax Act filed by Messrs. Manohar Lall-Deokaran Dass, proprietors of a ginning factory at Hansi, District Hissar, praying that the Income-tax Commissioner, Punjab, be required to state the case and to refer it to this Court on certain law points which arise in connection with the assessment of the petitioners for the year 1925-26. The points of law which the petitioners require to be stated are mentioned in paragraph 20-(a) to (i) of their petition. Most of these clauses attack the finding of fact arrived at by the Income-tax Officer (and confirmed by Assistant Commissioner) that the petitioners had deliberately withheld their account books. As this finding was based on evidence produced by the petitioners before the Income-tax Officer, no question of law arises in connection therewith. On this finding the following two questions of law arise:—

(1) Whether in view of the fact that the Income-tax Officer had already assessed the petitioners under section 23 (4) it was competent to his successor to reassess them under section 34 of the Act within one year from the original assessment, on the ground that their income, profits or gains chargeable to income-tax had escaped assessment; and (2) whether an order under section 23 (4) could be legally passed without hearing the evidence which the assesseees wanted to produce with regard to the profit of other factories at Hansi and without receiving their own *kachcha rokar* in spite of the fact that they had deliberately withheld the account books of their own factory for the period in question.

The first question has been judicially considered by this Court in *Balaki Shah v. Crown*(1), and answered against the contention of the assesseees. The Madras High Court has also taken the same view in *The Commissioner of Income-tax, Madras v. R. Sundaresa Aiyar*(2). After hearing Mr. Raj Kishan for the petitioners we are in agreement with the rule of law laid down in these rulings. Indeed, in my opinion, the wording of section 34 is not open to any other construction. We do not, therefore, consider it necessary to require the Commissioner of Income-tax to state the case on this point.

On the second point, in view of the finding of fact that at the time of the original assessment the petitioners failed to produce their account books and when notice was issued to them under section 34 they came forward with a story that their *'pakki rokar* and other necessary books had been lost in the train when the Manager of their factory was travelling from Hansi to Jind which story has been found to be wholly false, we think that the Income-tax Officer was justified in refusing to allow the petitioners to produce the evidence of the profits of the other factories or to receive the *kachchi rokar* of the peti-

(1) 1 I. T. C. 256.

(2) 2 I. T. C. 173.

tioners which would obviously be of no value in the absence of the *pakki rokar* and the ledgers.

This being our view on the two questions of law which arise in the case, we do not think it necessary to give a decision on the preliminary question raised by Mr. Jagan Nath Aggarwal for the respondent that this petition under section 66 (3) was incompetent. Having regard to all the circumstances of the case we leave the parties to bear their own costs in this Court.

(272) IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Mr. Justice Tek Chand and Mr. Justice Aga Haidar.

[5th December, 1928.]

Muhammad Hayat—Haji Muhammad

.. Assessee.*

v.

The Commissioner of Income-tax, Punjab and N. W. Frontier Province.

Income-tax Act (XI of 1922), Sec. 66 (3)—Application to Court for reference—Period of limitation—Exclusion of time for getting copy of Commissioner's order—Limitation Act (IX of 1908), Sec. 29.

In computing the period of limitation for an application under Sec. 66 (3) of the Income-tax Act the time spent in obtaining a copy of the Commissioner's order under Sec. 66 (2) can be excluded under Sec. 29 of the Limitation Act (as amended in 1922).

Application [Civil Misc. Petition No. 185 of 1928] under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) for an order to direct the Commissioner of Income-tax, Punjab and N. W. F. Province, to state a case for the opinion of the High Court.

Oertel, for the Assessee.

Jagan Nath Agarwal, for the Crown.

JUDGMENT.

This is an application under Sec. 66 (3), Income-tax Act by Messrs. Muhammad Hayat-Haji Muhammad, Sardar, of Patti, District Lahore, praying that the Income-tax Commissioner, Punjab, be required to refer certain question of law to this Court which arises from his order dated 17th August, 1927, relating to the assessment of income-tax for the year 1926-27.

A preliminary objection was taken by counsel for the respondent that the petition was barred by time. This objection is, however, devoid of all force. The order of the Commissioner under sub-sec. (2), Sec. 66 was passed on 17th August 1927, and under sub-sec. (3) of the same section this petition could have been filed within six months from the date on which the petitioner was served with notice of the aforesaid order. An application for a copy of the

* A. I. R. (1929) Lah. 170.

order of the Income-tax Commissioner was filed on 15th February 1928, and the copy was delivered to the petitioner on 12th March 1928. If the days spent in obtaining the copy be excluded, as they should be under Sec. 29, Limitation Act (as amended in 1922), the petition is within time.

The facts of the case, so far as they can be gathered from the various orders passed by the Income-tax authorities and the arguments at the Bar, are as follows:—The assessee has got a cotton ginning factory at Patti in the Lahore District. In compliance with the usual notice issued by the Income-tax Department he filed a return showing that in the 'previous year' he had suffered a loss of Rs. 8,689 on the working of the factory. The Income-tax Officer not being satisfied with the accuracy of the return, issued a notice under sec. 23 (2) on 3rd September, 1926, calling upon the assessee to attend on 23rd September 1926, and to produce or cause to be produced evidence on which he relied in support of the return. The hearing was subsequently adjourned from 23rd September, to 22nd October 1926. On that date the assessee appeared and produced his account books from 1st August 1925 to 31st March 1926, which he stated was the working season of the factory, and alleged that no accounts had been kept from 1st April 1926 to 31st July 1926 as in that period the factory was closed. The Income-tax Officer instead of calling for any other evidence and making the assessment under sec. 23 (3) issued a notice under sec. 22 (4) ordering the assessee to produce his account books for the remaining months of the previous year, i.e., from 1st April 1925 to 31st March 1926, and for three years prior to the 'previous year'. The assessee having failed to comply with this order the Income-tax Officer proceeded to assess him under sec. 23 (4) at an income of Rs. 70,000. An application under sec. 27 was made to have this assessment cancelled but was unsuccessful. An appeal to the Assistant Commissioner, Income-tax, also failed, whereupon the assessee moved the Commissioner to review the assessment under sec. 33 and also applied to him under sec. 66 to refer certain questions of law to this Court in the event of his refusal to review. Before passing orders, the Commissioner, however, called for a further report from the Income-tax Officer as to the data on which he had assessed the income at Rs. 70,000 under sec. 23 (4). The Income-tax Officer reported on 3rd August 1926, that he had arrived at that figure principally on information acquired in the course of enquiries made by him at Patti and Kasur from persons whose names he did not think it proper to put down in writing but which he was prepared to confidentially disclose to the higher authorities of the Department. On receipt of this report the Income-tax Commissioner rejected the application for review and refused to take action under sec. 66.

After hearing both counsel at length we are of opinion that on the admitted facts, the following two questions of law arise for decision, and we call upon the Income-tax Commissioner, Punjab, to state the case and refer it to the High Court with his opinion thereon:—

(1) In a case in which an assessee has duly filed a return of his income for the 'previous year', and has also, on receipt of a notice issued under sec. 23 (2), produced evidence in support of the return, including such account books as he possesses, but the Income-tax Officer is not satisfied with such evidence, should he proceed to make the assessment under sec. 23 (3), or can he at that stage issue a notice under sec. 22 (4), calling upon the assessee to produce his complete accounts for the 'previous year' and for three years prior thereto, and on the assessee's failure to do so, assess him under sec. 23 (4)?

(2) In making an 'assessment to the best of his judgment' under sec. 23 (4), does the Income-tax Officer possess absolutely arbitrary authority to

assess at any figure he likes, or is he to be guided by any judicial principles or rules of equity, justice and good conscience?

The parties shall bear the costs of to-day's hearing.

[273] IN THE COURT OF THE JUDICIAL COMMISSIONER, NAGPUR

FULL BENCH.

Before Mr. Findlay, Judicial Commissioner, Mr. Kinkhede and Mr. Prideaux,
Additional Judicial Commissioners.

[13th December, 1928.]

Sir S. M. Chitnavis, Kt.

.. Assessee.*

v.

The Commissioner of Income-tax, Central Provinces and
Berar

.. Referring Officer.

Income-tax Act (XI of 1922), Secs. 4, 6, 10 and 13—Money lending business—Accounts kept on mercantile basis—Assessee's option to write off bad debts—Limits of Income-tax Officer's authority—Renewal of debt bonds—Entry of interest due in interest Khata—Assessability as income.

An assessee keeping his accounts on the mercantile basis has the absolute option to write off a book debt as bad or irrecoverable at any time, whether before or after the period of limitation therefor, when he decides that the debt has become bad or irrecoverable. The Income-tax Officer has no authority to override the assessee's exercise of this right and to investigate or determine when in the Officer's opinion the debt became bad or irrecoverable.

The assessee, a money-lender keeping his accounts on the mercantile basis, in renewing his debt bonds credited the interest due thereunder in his interest Khata debiting the same to the accounts of the respective debtors. The assessee claimed that the interest credits not actually received or recovered in cash were not income assessable to income-tax.

HELD, that the interest credits in the Kasar (Interest) Khatas taken in conjunction with the debit entries in the debtors' personal accounts were merely expected receipts and unrealised assets of the business and not income, profit or gains assessable under the Income-tax Act.

Case [Misc. Judicial Case No. 33 of 1927] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Central Provinces and Berar for the opinion of the Court.

CASE.

Sir Shanker Rao Chitnavis, Kt., I.S.O., of Nagpur, had returned an income of Rs. 74,668 for assessment during the year 1926-27. This return was not treated as complete and after looking into the accounts, an assessment was made on an income of Rs. 1,16,480. Against this assessment an appeal was preferred and a few items were allowed as deduction by the Assistant Commissioner. The

* (1929) 25 N. L. R. 55 A. I. R. (1929) Nag. 50.

assessment then stood on an income of Rs. 1,13,012. In this amount are included two items:—

- (i) Rs. 7,481-13-9:—In all the assessee had claimed a deduction of Rs. 17,982 on account of bad debts. Of these, debts amounting to Rs. 10,105 were such as had fallen bad during the account year and were written off in that year and were allowed. Debts amounting to Rs. 7,481-13-9 were very old and had become bad on account of being time barred or otherwise such before the account year. They should have been written off in those years and were therefore not allowed.
- (ii) Rs. 16,031-4-6:—The assessee maintains his books on mercantile system of accountancy. As soon as the interest has accrued or as soon as the bonds are renewed, it is entered in the debtor's account and is taken as profit and is added to the Kasar Khata (Interest account). Seven debtors' bonds had been renewed during the year and the interest on them amounting to Rs. 16,031-4-6 was debited to their accounts and also credited to Kasar Khata. These bonds stated that the debts would be payable by instalments. For purposes of assessment the assessee sorted this out from the Kasar Khata and claimed that inasmuch as it was not actually received in cash it should not be taxed.

2. The assessee has now asked the following two points to be referred to the High Court:—

- (i) Has not the assessee got the option of declaring debts bad when he finds after sufficient waiting that from the circumstances of the debtors he is unable to recover them? Can the Income-tax authority deprive the assessee of this option? Should not the Income-tax Officer and the Assistant Commissioner have allowed Rs. 7,481-13-9 to the assessee on the same consideration on which the remaining amount out of Rs. 17,982 claimed by him was allowed?
- (ii) Could the Income-tax Officer and the Assistant Commissioner treat Rs. 16,031-4-6 on account of unrealized interest and merely credited in the books to equalize the sides of the Khata of the debtors, as 'income' coming into the hands of this assessee for the purposes of sections 4 and 6 of Income-tax Act and under ruling reported in 21 N. L. R. 175* especially when the major portion of the amount is made recoverable under the terms of the bonds in several future years? Can not the recoveries of this interest be taxed in future and not treated as income in the year under assessment?

(The Assistant Commissioner should have at any rate given a direction in his order that the future recoveries of Rs. 16,031-4-6 would not be taxed when these recoveries would be made).

Under section 66 (2) of the Indian Income-tax Act, I beg to refer the above points for the decision of the Hon'ble Judges of the High Court.

3. As regards the first point, I beg to say that the assessment is to be made on the income of the previous year. This is arrived at after making certain deductions or allowances specified in the Act. These deductions or allowances must also relate to the previous year. Expenditure, actual or

* Pandit Pandurang V. Commissioner of Income-tax, 2 I. T. C. 69.

notional that does not relate to the previous year cannot be allowed. The Act does not allow losses to be carried forward from one year to another. Bad debts are a form of notional expenditure and such expenditure must be deemed to be incurred when the debts become bad, that is, when they are found to be irrecoverable. When they become bad is a question of fact to be determined by the Income-tax Officer: It is clear, I submit, that an assessee cannot be allowed to accumulate bad debts and write them off in a year when he will escape the largest possible amount of income-tax by doing so. This answers the first two parts of the first question. The contention that the bad debts amounting to Rs. 7,481 should have been allowed on the same ground as the balance of the total claim of Rs. 17,982 was allowed, does not hold good inasmuch as the remaining debts became bad during the account year and were written off during that period and as such were correctly allowed. I submit therefore that this part of the question should be answered in the negative.

4. As regards the second question, I may say at the outset that the decision in the case of *Pandit Pandurang Ramchandra Pande, v. The Commissioner of Income-tax, Central Provinces*,⁽¹⁾ does not apply to this case. That case dealt with the interest that had not actually fallen due and determined no question relating to the manner of computing income; but simply said that the question involved in that case was a question of law. In this case the interest has already fallen due and is added to the interest Khata and what has been done is to assess the profits computed in the manner directed by section 13 of the same Act. I need not repeat here the arguments put forth at some length in the case of *Seth Nanhelal Ghasiram of Hoshangabad*,⁽²⁾ submitted to this High Court under this office letter No. H. C. R. 16/26-27, dated the 27th April 1927, showing how "constructive receipts" are taxable incomes and what led to the new provisions of section 13 of the Income-tax Act (XI of 1922) being brought on the Statute book. In a recent decision *The Commissioner of Income-tax, v. A. T. K. P. L. S. P. Subramaniam Chettiar*,⁽³⁾ the Full Bench of the Madras High Court have held that "when once an assessee has adopted the mercantile basis of accountancy, it is upon that basis, and upon that basis alone, that he is to be assessed." Hence the income of Rs. 16,031 derived from interest actually fallen due and entered in the Kasar Khata has been correctly assessed. This answers the second question. Regarding the assessee's observation that the Assistant Commissioner should at least have given a direction that this interest would not be taxed in future, it may be added that such a direction was entirely unnecessary since income that has once accrued or arisen (as this has) cannot accrue or arise again and cannot therefore become liable to tax again, so long as the petitioner adheres to the same system of accountancy. I submit that this question should be answered in the affirmative.

V. Bose and M. R. Bobde, for the Assessee.

D. N. Choudhari, for the Crown.

JUDGMENT.

KINKHEDE, A. J. C.:—This is a reference under section 66 (2) of the Indian Income-tax Act (XI of 1922). The following 2 points have been referred to this Court for decision by the Commissioner of Income-tax:—

- (1) Has not the assessee got the option of declaring debts bad when he finds after sufficient waiting that from the circumstances of the

(1) 2 I. T. C. 69.

(2) 2 I. T. C. 365.

(3) 3 I. T. C. 28.

debtors he is unable to recover them? Can the Income-tax authority deprive the assessee of this option? Should not the Income-tax Officer and the Assistant Commissioner have allowed Rs. 7,481-13-9 to the assessee on the same consideration on which the remaining amount out of Rs. 17,892 claimed by him was allowed?

- (2) Could the Income-tax Officer and the Assistant Commissioner treat Rs. 16,031-4-6 on account of unrealised interest and merely credited in the books to equalise the sides of the *khata* of the debtors, as 'income' coming into the hands of this assessee for the purposes of sections 4 and 6 of the Income-tax Act and under ruling reported in *Pandit Pandurang v. The Commissioner of Income-tax*,⁽¹⁾ especially when the major portion of the amount is made recoverable under the terms of the bonds in several future years? Can not the recoveries of this interest be taxed in future and not treated as income in the year under assessment?

2. The Commissioner of Income-tax has, in stating the case, answered the first question in the negative and the second in the affirmative.

3. The reference was originally heard by a Bench of two Judges of this Court on 10-4-1928, but as the questions raised were considered to be of such importance as to necessitate a decision by a Full Bench, the reference as a whole was set down for hearing by a Full Bench duly constituted. The points for decision concisely stated in the order of reference to the Full Bench are:—

- (1) When does a debt become a bad debt:
- (2) Whether sums entered as credits on account of interest and re-entered as debits in the assessee's accounts books—sums not actually received or proffered to the assessee—should be treated as income, profits or gains and should be taken into account in computing income for the year to which the entries relate?

4. A few facts which occasioned this reference under section 66 (2) of the Income-tax Act may be stated here. The assessee submitted a return showing Rs. 74,668 as his total taxable income for the previous year for purposes of assessment of income-tax for the ensuing year 1926-27. The income-tax Officer after looking into the accounts assessed him on an income of Rs. 1,16,480, but in appeal the Assistant Commissioner of Income-tax, Nagpur, reduced the assessable income to Rs. 1,13,012. This included Rs. 86,307-11-0 under the head of business profits taxable under section 10 of the Act. The assessee complains that in fixing the business profits at this amount the item of Rs. 7,481-13-9 out of a sum of Rs. 17,982 debited on account of bad debts was wrongly disallowed, and, the sum of Rs. 16,031-4-6 which represented unrealised interest, was wrongly treated as 'income' in the account year.

5. It will be seen from the Assistant Commissioner's order dated 25-4-1927 that in all Rs. 17,982 were claimed to be debited or written off as bad debts against the income of the account year. Lists were called for showing details of dates when these amounts had become due, with a view to ascertain when they were really found to be bad. On examination of the lists it was found that Rs. 7,481-13-9 were on account of old bad debts which had become

(1) 2 I. T. C. 69, 21 N. L. R. 176.

time barred long before the account year. The Assistant Commissioner overruled the contention of the assessee that it should be left to him to declare when particular debts became bad debts; and that the Income-tax Department should not go on presumption that the amount had become time barred in previous years. According to him the right criterion to know is to see whether and when the assessee's all legal remedies to recover it failed.

6. As to the other item of Rs. 16,031-4-6, the Assistant Commissioner has observed that this amount of interest is shown in the profit and loss account, i.e., *Kasar Khata* as interest receipts although no actual recovery was made; and that, as the assessee's books are on the book profit system and not on cash basis, the assessment has to be made on interest accrued and due, and it has nothing to do with what the assessee actually recovered. He opines that there can be no unfairness in this kind of assessment, because when bad debts are claimed interest is already included in them.

7. In stating the case the Commissioner has pointed out that this sum of Rs. 16,031-4-6 represented the interest which was debited to the accounts of 7 debtors whose bonds had been renewed during the year with corresponding credit to the *Kasar Khata*. These bonds are said to provide that the debts were payable by instalments in several future years.

8. Taking the point of bad debts first, I may refer to page 98 of Part III of Volume I of the Income-tax Manual, 2nd Edition, where in sub-paragraph (3) of paragraph 35, notes and instructions regarding the method of accounting for purposes of assessing income, profits and gains under sections 10 to 13 are set forth. It is pointed out there that "under the mercantile accountancy system.....an entry is made on the receipt side when a sale is concluded, although the money on account of such a sale has not been paid and in making up the accounts at the end of the year such entries are treated as receipts, and the tax is levied on these 'book profits'. It may happen that some of these 'book profits' cannot be recovered; they are written off as 'bad debts' when found to be irrecoverable; and since such 'book profits' have been included in the income assessed to income-tax, the 'bad debts' must be written off against the 'book profits' in the year in which they are written off in the accounts as irrecoverable. Where the cash system is adopted, there can be no 'bad debts'". I have underlined the important words.

9. On the statement of the Assistant Commissioner and the Commissioner that the assessee maintains his books on mercantile system of accountancy, the assessment of the business profits under section 10 of the Income-tax Act made by the Assistant Commissioner on Rs. 86,307-11-0 must be on what are treated as 'book profits' of the account year. It is, therefore, argued by the assessee's Counsel that if the tax is to be levied on 'book profits' he is entitled to write off against them, such book profits to the extent of Rs. 7,481-13-9 as have been found, or adjudged by him to be bad debts, and, as such irrecoverable in the account year. Even according to the aforesaid instructions where "'book profits' have been included in the income assessed to income-tax, the 'bad debts' must be written off against the 'book profits' in the year in which they are written off in the accounts as irrecoverable." I think that this line of reasoning based upon the instructions themselves ought to be assumed as correct. It entitles the assessee to urge that in deducing the taxable income in the shape of book profits of the account year the whole of the amount of bad debts written off by him in his account as irrecoverable in the account year must be deducted. The receipt side of the account represents the aggregate of receipts not merely

on account of the year's new business but also those on account of the accumulated balances of business carried over from past years' accounts and, therefore, the debits against it must necessarily comprise the balance of outstandings actually carried over to the next year's books of accounts, and also the aggregate of such balances of the past years' businesses as have either turned out to be bad or irrecoverable in that year, or, are considered by the creditor, for several reasons, to be unfit to be carried over any further.

10. It is common knowledge that no creditor, ordinarily, likes to write off a debt, and, thereby create evidence, in his own account books, of its having been treated by him as a bad and irrecoverable debt, unless he has lost all hope of its recovery, whether he has lost his limitation for a suit in respect of it or not. Amongst Hindu debtors a notion prevails that it is a sin to die indebted to others, and several instances of debtors executing bonds, and pro-notes, and even alienating joint properties for satisfaction of even time-barred debts are often noticeable in Courts. A creditor, therefore, naturally hesitates voluntarily to enter as given up a debt which, by change of circumstances, his debtor or even his legal representative may arrange, or, be expected, to pay even after the expiry of limitation. An entry in the creditor's account books writing off a debt as a bad debt in any particular year is under such circumstances likely to be interpreted by the debtor as *prima facie* good evidence of conduct on the part of the creditor wherefrom an abandonment of his right to demand it might reasonably be inferred so as to serve as a good answer to any future demand, on the occasion of any adjustment or fresh loan. Such an entry is, in my opinion, a conscious act on the creditor's part whereby he determines his election, once and for ever, to treat the debt referred to therein as bad or irrecoverable. It, therefore, stands to reason that the creditor must have full discretion in the matter; because, it is he, and, not the Income-tax Officer who knows, or must be deemed to know, the circumstances and risks as well as chances of recovery from his debtor. The Income-tax Officer, cannot, therefore, legally insist that the assessee must subordinate his own will or discretion and even his decision in the matter to his decision. The creditor, merely because he happens to be an assessee liable to pay income-tax to the Crown, cannot be asked completely to surrender his own judgment and allow it to be overridden by that of the Income-tax Officer.

In the absence of any legislation to that effect an Income-tax Officer cannot, in my opinion, dictate to the assessee that he must write off a certain amount due to him after the lapse of the prescribed period of limitation. Nor can he lay down that in a given set of circumstances the assessee will show the amount as outstanding, at his own risk, since it will no longer give him any right to set it off as a bad debt against his profits. The Hindu law does not recognise any rules as to the extinction of claims by efflux of time. *Ram Kishan Raj v. Chhedi Rai*(1). The older the debt the greater the responsibility of the descendants of the man who leaves the debt unpaid. Vrihaspati accordingly lays down: "The father's debt must be first paid, and next the debt contracted by the man himself, but the debt of the paternal grandfather must even be paid before either of these." Kanhaiyalal, J., in the Full Bench case of *Gajadhar v. Jagannath*(2), observed, at pages 782-83, that "The Hindu law did not recognize any rule of limitation for the recovery of debts. A debt may become irrecoverable under the law now in force by reason of the lapse of the period of limitation, but the debt exists all the same, and if a person chooses to pay a time-barred debt in the manner permitted by section 25 of the Indian Contract

(1) (1922) I. L. R. 44 All., 628.

(2) (1926) I. L. R. 46 All., 775.

Act, the debt which he chooses to pay remains the same debt, though by reason of the contract which he enters into, it assumes a new garb and gains a fresh vitality." Mere loss of limitation for a suit cannot, therefore, be regarded as a criterion of universal application in the matter of writing off debt.

11. Sometimes it may happen that when a loan is taken by a debtor he may be quite solvent and the creditor may entertain no doubt as to his ability to pay. In the next year of the advance, and, perhaps, several years before the due date, he may become involved in a financial crisis, for which he is not responsible, as a result of the bank or firm, with which he may have been crediting his surplus money, failing. There may thus be no prospect in that year, or in the near future, of any recovery from such a debtor. If as argued on behalf of the Crown, this creditor were to make it his practice to debit as bad or irrecoverable debt, every loan or its balance on the expiry of 3 years from its due date, and not earlier, how and when is he to debit the amount of the debt to the *Kasar Khata*, although he is quite satisfied as to the debtor's inability to liquidate it. Is he to wait until the whole debt falls due, and also for a period of 3 years thereafter, to become entitled to debit the said debt as a bad debt for purposes of income-tax? Or, should he debit it in the year in which the debtor's inability to pay became clear to his mind? The Income-tax Department might in the latter case come down on him for having departed from his system of book-keeping and may therefore disallow that debit. It is no use multiplying instances to expose the absurdity of the contention. Several anomalous results will follow, if the assessee's discretion or election in the matter of the choice of the proper time to write off a debt advanced by him, as a bad or irrecoverable debt, were allowed to be overridden by the taxing officer's decision in this way.

12. The assessee must for obvious reasons be the sole arbiter of his own rights and privileges as regards the business he conducts in his own interest. What is to his interest, and what is prejudicial to him, must depend upon his own decision. It, therefore, follows that, on the question whether to treat any particular debt as bad or irrecoverable, his word or decision must be final; for he alone is or can be the judge of the risks, chances and circumstances which may affect the recovery or non-recovery of that debt from his debtor.

13. There is nothing in the wording of section 24 of the Income-tax Act of 1922 which militates against this view. That section does not authorise the Income-tax Officer to investigate and determine the year in which any loss sustained is to be deducted from profits. All that it enacts is that the loss sustained in any year under any of the heads mentioned in the taxing sections shall be set off against his income, profits or gains under any other head in that year, so that loss under one head of income can be charged against profits under another in the same year. A reference to Lord Halsbury's Laws of England, Volume 16, paragraph 1310, dealing with the subject of income-tax, shows that in England no deduction is allowable "for any debts except bad debts proved to be such to the satisfaction of the Commissioners." I do not find such a prohibition either in section 10 or section 24 or anywhere else in the Indian Income-tax Act of 1922. In the absence of words "proved to be such to the satisfaction of the Commissioners" or words to that effect, in the Indian Statute, I am inclined to take the view that bad debts are deductible from business profits at the option of the assessee; the deduction need not be of only such as are proved to the satisfaction of the income-tax authorities to be bad debts. I do not find any restriction in the Indian Statute as to the year in which the bad debts could be deducted by the assessee. In the absence of words in the statute restricting

the assessee's option, and, prescribing the time for writing them off, or, the quantum of proof required, as a condition precedent, for doing so, or, imposing the condition that the income-tax authority should be consulted before writing them off, I think the assessee's right to debit the loss sustained on account of bad debts written off by him, against the profits or gains of any year, must be held to be unqualified and absolute, as regards the amount to be debited and the choice of time at which to write it off. His decision to write bad debts off the account cannot be regarded as conditional upon his proving them to be bad debts to the satisfaction of the Income-tax authorities, as is the case under the English Statute.

14. In the absence of any express provision in the Income-tax Act, 1922, either authorising or prohibiting the deduction of bad debts from the profits of a business carried on by an assessee, and in view of the fact that the specific directions in section 10 of the Act are subsidiary to the underlying principle that only profits, ascertained according to the mercantile system of accounting, are taxable, there can be no two opinions that bad debts actually written off the account as such by a creditor would form a proper deduction. What is usually done is to square up the debtor's personal ledger account by entering a corresponding credit to wipe out, wholly or partially, as the case may be, the debit standing against his name. Thus, once these personal ledgers of the debtors are squared up, or the balance due reduced by the amount written off, the sums so written off can no longer be carried over to the next year's books as outstanding assets of the business. These aggregate sums written off, must, therefore, necessarily go to reduce the receipts of the business profits in the year in which they are written off and thus reduce the balance of outstandings to be carried over to the next year. It, therefore, follows that, unless and until the bad debts are written off the account, no right to claim a deduction on their account, even though they may have been ascertained in the past years, accrues to the assessee. If the assessee has failed to sort out in the past the bad debts from the good or doubtful debts, and, indiscriminately carried over the whole of the outstandings to the next year's account, it does not stand to reason that he should be compelled for ever, at least for purposes of income-tax assessment, either to treat what are admittedly bad debts of some standing as good debts because of his omission to sort them at such time as the income-tax authorities may think, was the proper time for that purpose, or to take the risk of being called upon to pay tax on business profits by ignoring bad debts altogether. For these reasons I am of opinion that the item of Rs. 7,481-13-9 was wrongly disallowed in computing income under the head of "business profits."

15. I now proceed to consider the second point referred. As pointed out by the Bench of this Court in *Pandit Pandurang v. The Commissioner of Income-tax*(1), the word 'income' has nowhere been defined in the Income-tax Act of 1922. The learned Judges of the said Bench referred to the Privy Council decision in *St. Lucia Usines and Estates Co., v. St. Lucia*(2), and in particular to Lord Wrenbury's following observations as regards the true meaning of the word 'income' as used in the taxing statute which was involved in that case, and the provisions whereof are more or less analogous to those of the Indian Statute in this respect:—

"The words 'income arising or accruing' are not equivalent to the words 'debts arising or accruing.' To give them that meaning is to ignore the word 'income'. The words mean 'money arising or accruing by way of income.' There must be a coming in to satisfy the word 'income'. This is a sense which is assisted or confirmed by the word 'received' in the proviso at the end of section 4

(1) 2 I. T. C. 69; 21 N. L. R. 175.

(2) (1924) A. C. 508 at 512.

sub-section 1. If the tax-payer be the holder of stock of a foreign Government carrying say 5 per cent. interest, and the Government is that of a defaulting State which does not pay the interest, the tax-payer has neither received nor has there accrued to him any income in respect of that stock. *A debt has accrued to him but income has not.* It does not follow that income is confined to that which the tax-payer actually receives. Where income-tax is deducted at the source the tax-payer never receives the sum deducted but it accrues to him. It is said, and truly, that a commercial company, in preparing its balance-sheet and profit and loss account, does not confine itself to its actual receipts—does not prepare a mere cash account—but values its book debts and its stock in trade and so on and calculates its profits accordingly. From the practice of commerce and of accountants and from the necessity of the case this is so. But this is far from establishing that *income arises or accrues from* (as above instanced) *an investment which fails to pay the interest due.*"

I have underlined the words which seem to me to be important for the purposes of this reference.

16. In the aforesaid case their Lordships of the Privy Council had to interpret the words "accruing or arising" as also the words 'derived' or 'received' as used in relation to the words 'income, profits or gains' in an Income-tax Ordinance, 1910, of St. Lucia where also income-tax was leviable on an assessment made on the basis of a return of the assessee's income for the previous year, as is the case under the Indian Income-tax Act. Their Lordships hold that the appellant Company had not derived or received any 'income' in the account year, as the purchaser from that Company had not paid the interest payable in that year on the unpaid part of the purchased price which became due then. They thus distinguished 'income' from 'debt' (for the purposes of assessment) and held that the word 'income' is not equivalent to the word 'debt', and unless 'money arising or accruing by way of income' actually 'comes in', there is no 'income' in the strict sense of the term.

17. In *Gresham Life Assurance Society v. Bishop*(1), Lord Lindley has observed that a sum of money may be received in more ways than one, e.g., by the transfer of a coin or a negotiable instrument or other document which represents or produces a coin and is treated as such by business men. Even a settlement of account may be equivalent to a receipt of a sum of money although no money were passed. His Lordship further observed that to constitute a receipt of anything there must be a person to receive and a person from whom he receives, and something which is received by the former from the latter must be a sum of money, and that "a mere entry in an account which does not represent such a transaction does not prove any receipt, whatever else it may be worth".

18. If the principles underlying the two Privy Council cases quoted above for determining what is 'income' were applied to the facts and circumstances of this case, I think that, the arrears of interest, which were calculated and went to form the consideration of the several renewed bonds then accepted, having been allowed to remain unpaid and locked up again in the hands of the debtors for a further period stipulated in each bond, could not be treated as 'income derived, accruing, arising or received' at the time. To become 'income' of that year it had then to 'come in', which admittedly it had not. A mere entry in the account, therefore, under the *Kasar Khata*, with a view to equalise or square up the old debit of the amount outstanding against the debtor and, also to make fresh entries in the debtor's personal ledger account only to tally them with the terms of the contracts concluded in the shape of renewed bonds, does

(1) 4 Tax Cas. 464 ; (1902) A. C. 287.

not and cannot, in my opinion, entitle the debtor to say that the said amount or the interest included therein was paid by him to the creditor on the date the bonds were renewed. Since the amount of prospective *sawai* debited to the debtor's personal ledger account cannot be regarded as an outgoing sum of money advanced to him actually on the date he executed a bond for a consolidated sum, a mere credit of that *sawai* in the *Kasar Khata* cannot be treated as 'income' under that date. Similarly, arrears of interest included in the consideration of the renewed bonds and debited to the debtor's personal ledger account with a corresponding credit thereof to the *Kasar Khata* imports no 'out-going' or 'coming in' of any sum of money.

19. Moreover, the *sawai* as well as the interest though credited the same day in the *Kasar Khata* was admittedly payable in the future under the terms of the renewed bonds. Consequently, so long as the amount of *sawai* or interest so included in the consideration does not become overdue to the creditor, he cannot be regarded as having even realised it, as it were, for purposes of income-tax assessment, simply because he credits it in the *Kasar Khata*. If the terms of the contract disentitle the creditor from demanding the interest until after the lapse of a certain period of time, and if when interest becomes due, the creditor may not succeed in realising it, I think it would not be just and equitable to treat the unrealised interest although formally credited to the *Kasar Khata*, as income profits or gains derived, accruing or arising or received, for purposes of the Income-tax Act.

20. The mere conclusion of a contract is not always sufficient to yield a business profit. It is the performance of its terms that leads to the accrual of a claim to, or to the receipt of, profits of the business. If on the occasion of taking the renewal bond the creditor expressly agrees to give time to the debtor to pay up the arrears of interest at a future date, he by his own contract precludes himself from demanding or realising it at once, or even within a reasonable time usually necessary to cash a cheque on a banker. In other words, the test to be applied is, whether any profits in the shape of interest had become due to the creditor in such a manner as to be immediately available to him, in the account year so as to be capable of being received by him at his choice and pleasure. If the interest-money has become due to the assessee in the manner and in the sense that it was so completely under his control that, he, by an act of his will, could receive it in cash without greater trouble than is involved in cashing a cheque, then only it could be called 'income' such as would be liable to payment of tax, otherwise, not: Cf. Sadasiva Ayyar, J.'s observations in *Secretary to the Board of Revenue, Income-tax, Madras, v. Arunachalam Chettiar*(1). Although this Madras case was under the Act of 1918 and the present is a case under section 13 of the Act of 1922, it does not make any difference in the principle applicable. Simply because, while under section 5 of the Act, 1918, only 'income' was made chargeable to income-tax and under section 6 of the Act of 1922, not only 'income' but 'profits' and 'gains' are made chargeable, the addition of the words 'profits' and 'gains' makes no difference as regards the matter now under consideration as I will show in the following paragraphs.

21. In *Tora Gul Boi v. Commissioner of Income-tax*(2), the sale proceeds of goods sold in England by the Amir of Bukhara through a commission agent were credited to the agent's banking account in London and then transferred to his order at Bombay. There was no definite agreement fixing the rate of commission payable to the agent. The dispute as to the commission was settled in a suit at Peshawar in accordance with a compromise executed at Kabul and

(1) 1 I. T. C. 75 ; I. L. R. 44 Mad. 65 at 80.

(2) 2 I. T. C. 346 ; I. L. R. 8 Lah. 335.

the Peshawar Court decreed that 2 lacs of the sale price was the property of the agent. The agent was assessed to income-tax on that sum. On the question being referred to the High Court at Lahore as to whether the Peshawar Court's decree resulted in the receipt by the assessee of the 2 lacs in British India for purposes of section 4 (1) of the Indian Income-tax Act of 1922, it was held that as the assessee had received the price for the goods in England *not* as owner but merely as agent, notwithstanding his right to detain a portion of the money as his remuneration, he was not competent to convert the same to his own use before he had settled with the Amir, and thus, for the purposes of Indian income-tax, the assessee received his 2 lacs after it had been allotted to him by virtue of the compromise.

22. In *J. P. Hall & Co., Ltd. v. The Commissioners of Inland Revenue*(1), it was held, that, for the purposes of Excess Profits Duty, profits from the contracts for the purchase and sale of the control gear arose to the appellant Company in the accounting periods in which the gear was actually delivered and not in the pre-war period ending the 30th June 1914, in which the contracts were made. The following observations of Lord Sterndale, M.R. are important:—
 “.....these profits were neither ascertained nor made at the time that these two contracts were concluded. There are any number of contingencies that might have happened, by which the profit would not have turned out what it appeared on the face of it when the contracts were made. Any number of complications might have occurred that might have caused quite a different result to have accrued from these two contracts.” Atkin, L. J., also observed that “The profits for Excess Profits Duty are to be assessed on the same basis as profits for Income-tax purposes, and the word ‘profits’ for Income-tax purposes is to be understood in accordance with the words of Lord Halsbury in the *Gresham Life Assurance Society v. Styles*(2) ‘in its natural and proper sense, in a sense which no commercial man would misunderstand’, and he says ‘that profits and gains must be ascertained on ordinary principles of commercial trading.....’. It seems to me that no person here trying to ascertain these profits on the principles of ordinary commercial trading would dream of including profits in his yearly balance-sheet, which would not be made until the goods had actually been delivered in respect of some contract which was to run over a period of at least two years, possibly more. To my mind the procedure of the company was the ordinary commercial procedure in taking the profits that they made as and when the goods were delivered. Anything else, it appears to me, would be quite contrary to commercial procedure, and would not be profits in the natural and proper sense.”

23. The principles deducible from these rulings are that unless and until the preliminary conditions necessary for earning the benefit of any business contract as a profit are settled, or performed, the profit does not even arise, or accrue. To treat it as a profit, in its real sense, the assessee must be ‘competent to convert the same to his own use’; he cannot, therefore, be regarded as having received any income in the shape of profits of the particular business contract until the contract is performed. Further a mere conclusion of a contract is not sufficient, nor will a receipt of money on somebody else account be sufficient pending settlement with him. It, therefore, follows that a mere credit of the amount of interest in the *Kasar Khata*, in the year when the contract is concluded, pending the actual receipt thereof after it falls due, is not sufficient to charge the amount so credited as ‘income’. Not only this but a credit of the anticipated profit in the very year in which the contract is made, i.e., before the

(1) 12 Tax Cas. 882.

(2) 8 Tax. Cas. 185, at pp 188 and 189.

performance, or delivery, contemplated by it, falls due, or, is given, is 'contrary to commercial procedure' and would not reflect the real 'income' of the assessee, or 'be profits in the natural and proper sense.'

24. Reading the credit entries in the *Kasar Khata* in conjunction with the debit entries in the debtor's personal ledger account, the only legal inference deducible therefrom is that what is shown as received under the *Kasar Khata* is really not received at all but is only expected to be received or perhaps may never be received and the amount so credited can therefore be regarded merely as an unrealised asset of the business, and not as 'income' or 'profits' or 'gains' of the business. What is only a *jama khardhi kasar*, i.e., profit by book adjustment cannot be confused with profit derived from cash realisations of interest, merely because both are lumped together under one ledger head *Kasar Khata*.

25. A Bench of this Court had occasion to decide in *Seth Nanhelal v. Commissioner of Income-tax*,⁽¹⁾ a more or less similar question upon a reference by the Commissioner of Income-tax. It was there held that sums shown in the accounts as having fallen due but not received could not be treated as 'income'. I think that the said decision in no way contravenes the provisions of section 13 of the Income-tax Act of 1922. For these reasons, I am of opinion that the item of Rs. 16,031-4-6 which represents unrealised interest was wrongly treated as 'income', 'profits' or 'gains' under the head of 'business' by the Assistant Commissioner of Income-tax in taxing the present assessee.

26. As a result of the above conclusions I recommend that the answer to the first point should be in the affirmative, and that to the second should be in the negative.

PRIDEAUX, A. J. C.:—I have had the advantage of perusing the opinion of Kinkhede, A. J. C., in this case and I agree with him in his decision on both questions.

FINDLAY, J. C.:—I have had the advantage of perusing the opinion of Kinkhede, A. J. C., in this case and I fully concur therein.

ORDER.

FINDLAY, J. C. AND STAPLES, A. J. C.:—(1) Under section 66 (2) of the Indian Income-tax Act of 1922, the Commissioner of Income-tax referred to this Court the two questions raised in paragraph 2 of his statement of the case relating to the liability or otherwise of the non-applicant Sir S. M. Chitnavis to certain deductions from his income, which were in dispute.

(2) The Bench consisting of Prideaux, A. J. C., and Findlay, J. C., saw cause, because of the importance of the two matters involved, to refer the whole question to a Full Bench, vide the order of 13th April 1928 of the Bench and the order of reference made by the Judicial Commissioner on the same date.

(3) The Full Bench have now delivered an unanimous opinion on the points involved on the 6th instant and, in accordance with the said opinions, we answer the two questions referred to us as follows:—

(1) The assessee has the option of declaring debts bad when he finds, after sufficient waiting, that, from the circumstances of the debtors,

he is unable to recover them. As the law at present stands, the income-tax authority cannot deprive the assessee of this option. The present non-applicant was, therefore, entitled to the deduction of Rs. 7,481-13-9 on the same consideration on which the balance of the amount of Rs. 17,892 was allowed; and

- (2) The Income-tax authorities were not entitled to treat the amount of Rs. 16,031-4-6 on account of unrealised interest as income for the purposes of sections 4 and 6 of the Income-tax Act. The recoveries of this item of interest can be taxed in the future and cannot be treated as income in the year under assessment in this case.

4. These findings dispose of the reference. We order that the applicant (Commissioner of Income-tax) should pay the non-applicant's costs in these proceedings and we fix the amount of costs at Rs. 150.

(274) IN THE COURT OF THE JUDICIAL COMMISSIONER, NAGPUR.

Before Mr. Findlay, Judicial Commissioner.

[20th December, 1928]

Dr. Sir Hari Singh Gour

.. Assessee.

v.

The Commissioner of Income-tax, Central Provinces and Berar.

Income-tax Act (XI of 1922), Secs. 10 (2) (ix) and 66 (3)—Motor car expenses of a lawyer—Sums spent in replacement of old law books—If admissible deductions—Proper house rental value, if a question of law.

Expenditure incurred by a lawyer in the maintenance of a motor car not shown to have been kept solely for professional purposes is not permissible allowance in the computation of his assessable income.

Money spent by a lawyer in replacing old editions of law books by new ones is capital expenditure and hence is not an admissible deduction.

The question of the proper rental value of house property is not a question of law for a reference to the High Court under Sec. 66 (3) of the Income-tax Act.

Application [Misc. Judicial Case No. 61 of 1928] under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) for an order directing the Commissioner of Income-tax, Central Provinces and Berar, to state a case for the opinion of the Court.

M. R. Bobde, for the Assessee.

D. N. Chowdhari, for the Crown.

JUDGMENT.

(1) This is an application under section 66, sub-section (3) of the Income-tax Act, requesting this Court to order the Commissioner of Income-tax to state

a case with reference to the matters marked as No. (3) (i), (ii) and (iii) in the application, dated 28-5-1928, of Sir Hari Singh Gour to the Commissioner of Income-tax. The latter has assented to the other points raised in the said application being referred to this Court but declined to refer the three points I am concerned with on the ground that they were questions of fact and not questions of law.

(2) The first point is concerned with the Income-tax Commissioner having assessed the bungalow occupied and owned by Dr. Gour at a rental of Rs. 200 per month, that is, Rs. 2,400 a year. The only position taken up by the assessee in this connection was that he made an admission that the Municipal assessment of the bungalow was Rs. 1,800 only, and what is urged here is that, in the absence of any evidence to the contrary, the figure of Rs. 1,800 should have been accepted. I fail completely, however, to see how any question of law is involved here. The detailed provisions of the Evidence Act do not, in my opinion, apply to proceedings like those in question. It is, moreover, in the present case quite incorrect to say that the Commissioner of Income-tax had no material on which to hold that the bungalow would fetch a rental of Rs. 200 a month. It is clear from his statement of the case that the rental of Rs. 200 a month was arrived at by comparison of the rentals of other bungalow property in the neighbourhood and I may add to this that in the case of a bungalow owned by the occupant, the assessed rent for Municipal purposes is normally a much lower one than the actual market rent of the bungalow. In those circumstances, there is, in my opinion, no question of law at all involved in this connection and I see no reason to interfere.

(3) The next point urged on behalf of the applicant relates to the expenditure of Rs. 1,800 incurred on the yearly maintenance of a motor-car. Here, again, the application seems to me one without any substance whatever. It is, in the nature of things, impossible to suppose that the motor-car in question is kept solely for the purposes of the assessee's profession as a lawyer. It was indeed, to all intents and purposes, admitted in the course of argument that the car in question is used for other purposes and, in the very nature of things, it would be absurd to suppose that this was not so. Under the terms of sub-section (2) of section 11 of the Income-tax Act, therefore, the allowance in question was clearly not claimable by the assessee.

(4) As regards the claim of Rs. 1,200 for the replacement of old editions of law books by new ones, the Commissioner of Income-tax pointed out that no evidence had been produced in this connection and that, on this ground alone, it would have to be disallowed, but he went further and pointed out that, in any event, such expenditure fell under the head "capital" and could not be allowed for. It has been suggested that it was not necessary for the assessee to have produced evidence in this connection, but it is clear that notice was given to him to appear and produce evidence, if he so desired, and none was produced. Over and beyond this, however, I am wholly unable to understand how this item of renewal of books could be claimed. The old books remain the assessee's property and are not necessarily valueless while the expenditure on new books obviously falls under the head of "capital expenditure". Clearly, as regards this matter also no question of law is involved.

(5) The third point relates to the costs of preparing manuscripts for the press. That point is, it is true, connected with point 1 which has been referred to this court, viz., whether income from books can be classed as professional income or not. The present item, however, was disallowed for a perfectly

valid and proper reason, viz., that there was no proof whatever of it. What the assessee did was to estimate his net income only. Clearly, in the circumstances, the Income-tax Commissioner was within his rights in disallowing this item and no question of law arises there in view of the reason given for its disallowance.

(6) The application, therefore, fails on all points and is dismissed. The applicant must pay the costs of the Commissioner of Income-tax, the non-applicant, and I fix these at Rs. 50.

(275) IN THE HIGH COURT OF JUDICATURE AT RANGOON.

*Before Sir Guy Rutledge, Kt., Chief Justice, Mr. Justice Carr and
Mr. Justice Brown.*

(3rd January, 1929).

R. M. P. Chettyar Firm

.. Assessee.*

v.

The Commissioner of Income-tax, Burma

.. Referring Officer.

Income-tax Act (XI of 1922), Secs. 22 (2), (4) and 23 (4)—Submission of return by assessee—Subsequent notice under Sec. 22 (4)—Assessment for non-compliance under Sec. 23 (4), Validity of.

After an assessee has made a return of his income under Sec. 22 (2), an assessment can be made under Sec. 23 (4) for non-compliance with the terms of a notice under Sec. 22 (4).

Kam Khelwan Ugamlal v. Commissioner of Income-tax, 3 I. T. C. 225; Harmukhrai Dulichand v. Commissioner of Income-tax, 3 I.T.C. 198; Chandra Sen Jaini v. Commissioner of Income-tax, 3 I. T. C. 17; Followed.

Case [Civil Reference No. 10 of 1928] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Burma, for the opinion of the High Court.

CASE.

This reference is made to the High Court under the provisions of section 66 (2) of the Indian Income-tax Act on the application of the R. M. P. Chettyar firm, Gyobingauk, in connection with the firm's assessment for the year 1927-28.

The questions in respect of which a reference is sought by the applicant-firm are reproduced below:—I. Whether the Income-tax Officer is entitled to assess an assessee under section 23 (4) of the Act for an alleged default to comply with a notice under section 22 (4) after the said assessee has made a return and when no default under section 23 (2) is alleged. II. Whether in the present case it was open to the Income-tax Officer to make a valid assessment under section 23 (4) of the Act.

* (1929) I. L. R. 7 Rang. 26, A. I. R. (1929) Rang. 88.

The applicant's legal representative, at the hearing given in connection with the above application, admitted that the two questions are really concerned with the same point. They involve a question of law which may be referred in the following terms:—"After an assessee has made a return of his income under section 22 (2), can the assessment be made under section 23 (4) of the Act for non-compliance with the terms of a notice under section 22 (4)?"

2. The facts of the case relevant to this question are as follows:—

For the applicant-firm's assessment for 1927-28, which is the assessment in question, a notice under section 22 (2) was served on the firm's agent on the 6th July 1927. The agent submitted a return on the 30th July 1927, declaring an income of Rs. 14,330. The Income-tax Officer after receipt of this return issued notices under sections 22 (4) and 23 (2) for the production of all the accounts of the firm for the year 1926-27 and also for the attendance of the firm's agent or representative. In response to these notices, the agent appeared and produced certain account books. These account books were scrutinized. The result of this scrutiny showed that the books produced were not the complete books maintained in connection with the ordinary business of the firm. The Income-tax Officer therefore held that the applicant-firm failed to comply with the notice under section 22 (4) and for this default he made the assessment under section 23 (4) of the Act.

3. The questions reproduced above are raised by the applicant-firm in view of certain pronouncements and conflicting decisions by other High Courts in India.

In the case of *Brij Raj Rang Lal v. Commissioner of Income-tax, Behar and Orissa*(1), the Patna High Court, in dealing with the construction of sections 22 (4) and 23 (4) of the Income-tax Act, expressed the view that accounts or documents can be called for by the Income-tax Officer under section 22 (4) after issue of notice under section 22 (2) and before the filing of the return, and that after the filing of the return the Income-tax Officer should proceed under sections 23 (2), 23 (3) and 37 to secure whatever accounts or documents he may require. Proceeding on this construction, the High Court took the view that non-compliance with a notice under section 22 (4) where such notice is issued after the receipt of the return does not authorise the Income-tax Officer to make a summary assessment to the best of his judgment under clause (4) of section 23.

The same view was taken by the Lahore High Court in the case of *Khushi Ram Karan Chand v. Commissioner of Income-tax, Punjab*(2). But the Allahabad High Court in *Chandra Sen Jaini v. Commissioner of Income-tax, United Provinces*(3), dissented from this view.

The Calcutta High Court, also, on a reference made by the Commissioner of Income-tax, Bengal, under section 66 (2) of the Income-tax Act *Harmukhrai Dulichand v. Commissioner of Income-tax, Bengal*(4), held that the power given to the Income-tax Officer by section 22 (4) to call for accounts is not impaired by anything in section 23 (4) and that non-compliance with a notice under section 22 (4) issued at any time in the course of the assessment constitutes a default necessitating the application of section 23 (4). Subsequent to this judgment, the *Brij Raj Rang Lal* case (1) was reconsidered by a Bench

(1) 2 I. T. C. 418

(2) 2 I. T. C. 517

(3) 8 I. T. C. 17

(4) 8 I. T. C. 198

of the Patna High Court, and the decision, following that of the Calcutta High Court was that the decision in the *Brij Raj Rang Lal* case, in so far as it was a decision on the construction of section 22 (4), was wrong.

4. Under the Act, I am required to give my opinion on the question at issue in this case. The relevant portion of section 22 (4) of the Act is as follows:—
“The Income-tax Officer may serve on the principal officer of any company or on any person upon whom a notice has been served under sub-section (2) a notice requiring him, on a date to be therein specified, to produce, or cause to be produced, such accounts or documents as the Income-tax Officer may require.”

The only condition to be fulfilled for the valid employment of this provision is that, except in the case of a company, a previous notice under section 22 (2) requiring the submission of a return should have issued. No other condition is imposed or contemplated.

The other relevant provision of the Act is section 23 (4) which enacts:—
“If the principal officer of any company or any other person fails to make a return under sub-section (1) or sub-section (2) of section 22, as the case may be, or fails to comply with the terms of a notice issued under sub-section (4) of the same section or, having made a return, fails to comply with all the terms of a notice issued under sub-section (2) of this section, the Income-tax Officer shall make the assessment to the best of his judgment.”

There are three categories of default which make an assessment under this sub-section obligatory:—(1) Failure to make a return; (2) Failure to comply with a notice under section 22 (4), and (3) Failure to comply with a notice under section 23 (2).

These are three distinct categories, and if there is a default under any one of them, the Income-tax Officer must make the assessment under section 23 (4). The only disturbing element in the acceptance of this view in the cases referred to above was the existence of the words “having made a return” in section 23 (4). In my opinion, these words have no reference whatever to the power conferred on the Income-tax Officer by section 22 (4), nor do they have the effect of excluding from the purview of section 23 (4) a default under the second category after a return is made. They simply indicate that a notice under section 23 (2), and therefore a default in respect of it, can only eventuate after a return has been filed.

I am of opinion, therefore, that the question referred should be answered in the affirmative.

Foucar, for the Assessee.

Government Advocate, for the Crown.

JUDGMENT.

This is a reference made by the Commissioner of Income-tax under section 66 of the Indian Income-tax Act (XI of 1922), the question referred being:—“After an assessee has made a return of his income under section 22 (2), can the assessment be made under section 23 (4) of the Act for non-compliance with the terms of a notice under section 22 (4)?”

The essential question raised in the argument before us is whether a notice under section 22 (4) may or may not be issued by the Income-tax authorities after the assessee has made a return of his income as required by a notice under section 22 (2).

The assessee's contention that a notice under section 22 (4) can be issued only before a return has been made receives some support from the case of *Brij Raj Ranglal v. Commissioner of Income-tax*(1), and that of *Khushi Ram Karam Chand v. Commissioner of Income-tax*(2) neither of which appear in the authorised reports. But the first of these decisions has been expressly overruled by a full Bench of five judges of the same court—the High Court of Patna—in *Ram Khelawan Ugam Lal v. Commissioner of Income-tax*(3), and the same view was taken by the two other judges of the Court who referred the question to the full Bench. Thus seven judges of that Court are of opinion that the decision in *Brij Raj's*(1) case was wrong.

The same question has been considered by the High Court of Calcutta in *Harmukhrai Dulichand v. Commissioner of Income-tax, Bengal*(4), and by the High Court of Allahabad in *Chandra Sen Jaini v. Commissioner of Income-tax, U. P.* (5), and both of these Courts are in agreement with the decision in *Ram Khelawan's*(3) case. That being so the weight of authority is very strongly against the contention advanced by the assessee. The question has been very fully discussed in the judgments quoted and we agree with the arguments there set out and with the decision arrived at. We consider it unnecessary, therefore, to enter into further discussion of the question.

We answer the question referred in the affirmative.

The assessee must pay the costs of this reference—Advocate's fee 5 Gold Mohurs.

(276) IN THE HIGH COURT OF JUDICATURE AT RANGOON.

Before Sir Guy Rutledge, Kt., Chief Justice, Mr. Justice Carr and Mr. Justice Brown.

[3rd January, 1929.]

Somasundaram Chettiar

.. Assessee.

v.

The Commissioner of Income-tax, Burma

.. Referring Officer.

Income-tax Act (XI of 1922), Secs. 22 (4), 23 (4), and 66 (3)—Foreign Firm with branch in Rangoon—Rangoon branch purchasing for foreign branch—Asst. under Sec. 23 (4) on non-production of foreign branch accounts, Legality of—Jurisdiction to call for foreign accounts.

The assessee, a foreign firm with head-quarters in Pudukottah State and branches at Alleppey and Jaffna, had a branch at Rangoon doing banking and money-lending business. On occasions the Rangoon branch purchased rice and consigned it to Alleppey and Jaffna branches. On failure to produce the Alleppey and Jaffna branch accounts requisitioned under Sec. 22 (4) of the Income-tax Act, an assessment was made under Sec. 23 (4).

On an application under Sec. 66 (3), the High Court directed the Commissioner of Income-tax to state a case on the question whether it was open to the Income-tax Officer to require the production of Alleppey and Jaffna branch accounts and in default of their production, to make an assessment under Sec. 23 (4).

(1) 2 I. T. C. 458

(3) 3 I. T. C. 225

(5) 3 I. T. C. 17

(2) 2 I. T. C. 517

(4) 3 I. T. C. 198.

Case [Civil Miscellaneous Application No. 70 of 1928] stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income tax, Burma, for the opinion of the High Court.

CASE.*

In pursuance of the order of the High Court of Judicature, Rangoon, dated the 24th August 1928, in Civil Miscellaneous Application No. 70 of 1928, the following case is stated for the decision of the High Court under the provisions of section 66 (3) of the Indian Income-tax Act, 1922.

2. The P. K. N. Chettyar firm which is the applicant in the present case has questioned the legality of an assessment made on it for the year 1925-26, under the provisions of section 23 (4) of the Indian Income-tax Act, on several grounds. The order of the High Court in question directs me, however, to state and refer the case with reference to one of the grounds on which the validity is contested, namely, the contention that, the assessee having made a return, the assessment under section 23 (4), for non-compliance with the terms of a notice issued under section 22 (4), is invalid. Precisely the same question has been raised in other High Courts in India and, in view of conflicting decisions, this Hon'ble Court has directed that the question should be stated for a ruling by it.

The question may be set out as follows:—"After an assessee has made a return of his income under section 22 (2), can the assessment be made under section 23 (4) of the Act for non-compliance with the terms of a notice under section 22 (4)?"

* * * * *

Foucar, for the Assessee.

Eggar, Government Advocate, for the Crown.

JUDGMENT.

This is a reference made by the Commissioner of Income-tax in compliance with a mandamus issued by this Court under section 66 (3) of the Indian Income-tax Act. The question referred, namely "After an assessee has made a return of his income under section 22 (2), can the assessment be made under section 23 (4) of the Act for non-compliance with the terms of a notice under section 22 (4)?"

In *R. M. P. Chettyar Firm v. Commissioner of Income-tax, Burma*(1), we have today answered this question in the affirmative and therefore no further discussion of it is necessary.

But the assessee contends that the referring of this question only is not a sufficient compliance with the directions of this Court.

The assessee is the P. K. N. Chettyar Firm, which, it is claimed, is a foreign firm, having its head-quarters at Visvanathapuram in Pudukottah State. It has also branches not in British India at Jaffna, Alleppey, Moovar and Malacca. It has a branch in Rangoon which carries on a banking and money-lending business, but this part of the business does not appear to be in question in the present controversy. This branch on occasions purchases rice in Rangoon and consigns it to the Jaffna and Alleppey branches. The Income-tax Officer served the assessee, under section 22 (4) of the Act, with a notice to produce the accounts of the Jaffna and Alleppey branches and on his failure to comply with that notice made the assessment under section 23 (4).

* Paragraphs 3 and 4 omitted here are identical with paragraphs 3 and 4 of the case in the preceding connected case of *R. M. P. Chettyar Firm* printed at page 335.

(1) 3 I. T. C. 335.

Essentially the assessee's contention is that the accounts called for are foreign accounts which he cannot be required to produce, that the notice under section 22 (4) was therefore *ultra vires*, and that failure to comply with it is not a default which entitles the Income-tax Officer to make the assessment under section 23 (4). He did, in his application, for a mandamus, also raise the question which has actually been referred.

The first question before us is of the construction of the order issuing the mandamus, and it must be admitted that the intention of the learned judges is not altogether clear. On the one hand they said:—"The Commissioner held that the only question for determination was whether the assessee's refusal to produce his books was a good reason for making the assessment under section 23 (4). He was of opinion that the answer was so obvious as not to call for a reference. In view of the fact that the firm is not resident in British India, and that the agent in Rangoon merely purchased rice under orders in Rangoon for shipment to Jaffna, the question of whether the Rangoon agent could be called upon to produce the books of the Jaffna and Alleppey branches is perhaps not quite so simple as the Commissioner thought."

This paragraph suggests that the learned judges thought that the contention of the assessee was one that should be considered by the Court.

On the other hand they went on to say:—"The points on which a reference is desired are:—

(1) whether the assessment has been legally made under section 23 (4), and (2) whether the assessee can be denied his right of appeal where he denies the liability to be assessed (a) as an unregistered firm, (b) on the foreign income of his non-resident principals, (c) as a successor to P. K. N. C. T."

They then referred to certain conflicting decisions which we have considered in *R. M. P. Chettyar Firm v. Commissioner of Income-tax, Burma*(1), and finally said:—"In view of the conflicting decisions we consider it desirable that the question should be settled by a ruling of this Court. We accordingly direct that the Commissioner of Income-tax do state and refer the case with reference to the question whether the assessment has been legally made under section 23 (4). We do not consider that the other points which we are asked to have referred call for an independent Reference."

Now the conflict between the decisions mentioned was on the question whether a notice under section 22 (4) of the Act can be issued after the assessee has made a return of his income—that is, on the question which the Commissioner has now referred. The form of the final order therefore rather suggests that the learned judges intended that only that question should be referred.

But reading their judgment as a whole we think that the question whether the Income-tax Officer had the power by a notice under section 22 (4) to require the production of the books of branches not in British India of a firm that is itself a foreign firm is in fact included in the question of the legality of the assessment. If the officer had not that power, then it would seem that failure to comply with an illegal notice cannot be treated as a default rendering the assessee liable to assessment under section 23 (4).

We think also that this is a question of law of very considerable importance and that it should be decided. We note that the case of *Duni Chand v. The Commissioner of Income-tax*(2), has some bearing on this question.

We therefore answer the question referred in the affirmative, for the reasons given in *R. M. P. Chettyar Firm v. Commissioner of Income-tax, Burma*,(1).

We direct further that the Commissioner of Income-tax do state the case and refer to this Court the further question whether, in the circumstances of this case, it was open to the Income-tax Officer to require the production of the books of the Jaffna and Alleppey branches of the assessee; and, if not, whether the failure to comply with such a requisition is a default within the meaning of section 23 (4) of the Act and renders the assessee liable to assessment under that sub-section. Costs reserved.

(277) IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Mr. Justice Zafar Ali and Mr. Justice Addison.

[7th January, 1929]

Messrs. Kalu Mal—Shori Mal

.. Assessee.*

v.

The Commissioner of Income-tax, Punjab and N. W.
Frontier Province

.. Referring Officer.

Income-tax Act (XI of 1922), Secs. 25 (3) & 26—Partition of Hindu joint family—Family business allotted to one member—Business subsequently carried on under old name—Business, if discontinued—Assessment as successor.

On a partition of a Hindu joint family, the assessee got the family business as his share, the other co-parceners, the assessee's sons, relinquishing their rights therein and starting separate businesses of their own. The assessee continued to carry on the business under the old name and style, retaining the account books with the right of realising the business outstandings.

HELD, on the facts of the case that there was no discontinuance of the business within the meaning of Sec. 25 (3) of the Income-tax Act and that as a result of the partition the assessee succeeded to the family business within the meaning of Sec. 26.

Case (Referred Case No. 40 of 1927), stated under Sec. 66 (3) of the Indian Income-tax Act, (XI of 1922), by the Commissioner of Income-tax, Punjab and N. W. Frontier Province for the opinion of the High Court.

CASE.

The facts of the case are as follows:—The petitioner, L. Nathoo Mal, carries on a business in dyes at Amritsar, Multan, Cawnpore and Bombay, under the name and style of "Kaloo Mal Shori Mal and Co." Till the 19th April 1923, he did this business along with his sons, as the head of a Hindu undivided family. On that date, there was a family partition and his six sons relinquished their rights in the business, which thence-forward was carried on by L. Nathoo Mal as sole proprietor and the sons started separate businesses of their own. In connection with its assessment for 1923-24, he applied for the benefit of Sec. 25 (3) of the Income-tax Act on the ground that the partition involved the discontinuance of the business. It was held, however that there was no discontinuance but only a change of ownership and that, therefore section 26 applied. I was asked to refer the question to the High Court, but declined, as it seemed to me one of fact. By an order dated the 22nd June, I have now been directed to state a case as to what is the legal effect of the disruption of the family.

* A. I. R. (1929) Lah. 461 (3).

2. It is common ground that the case is governed either by section 25 (3), or by section 26; and it is not disputed by the department that if the partition resulted in the discontinuance of the business, section 25 (3) applies; nor by the petitioner, that if section 26 applies, the assessment was correctly made. The question, therefore, resolves itself into whether or not the business was discontinued.

3. To determine this, we must look to the conditions of the partition. These are stated in two deeds of relinquishment executed by the petitioner's sons on the 19th April 1923, the date of the partition. Copies of the deeds are attached and marked Exhibit A* and Exhibit B*. In Exhibit A, which is executed by the petitioner and four of his six sons it is stated that the four sons have been, or would be given (a) certain immoveable property, (b) dyes to the value of two lakhs, and (c) two lakhs of rupees in cash, in return for which it is agreed that they and their heirs "have and shall have no right..... upon the firm known and styled as Kaloo Mal Shori Mal and Co., and other firms including or excluding our names, and furniture, debts and credits of the firms." It is further stated that the account books belong to L. Nathoo Mal, that the sons have no right to remove them and that they "have no connections with the amounts" entered in them, and finally, that the deed of relinquishment gives up, "all the concerns in favour of L. Nathoo Mal". Exhibit B was executed by L. Nathoo Mal and the two remaining sons. The consideration is the same as before varying only in amount, and the terms of relinquishment are virtually identical. The only passage that need be quoted is the undertaking given by the sons that "whatever business we shall do from to-day we shall do that separately under our own name."

4. These deeds need only be considered so far as they concern the business of Kaloo Mal Shori Mal and Co., and as it was no part of this business to deal in immovable property, the partition of the latter does not affect the issue. The whole business, a very extensive one, was handed over to L. Nathoo Mal, subject to certain payments in cash and in kind, which, however, had not to be completed for 21 months. These payments did not involve the closure of any branch, nor did they affect the goodwill of the business which passed to the petitioner. The business, therefore, remained intact and the only change made by the partition was to transfer it from the petitioner's family to the petitioner himself. In my opinion, therefore, there was no discontinuance, but only a succession to ownership on the part of L. Nathoo Mal. This view is supported by the case of the *Commissioner of Income-tax v. M. H. Sanjana and Co., Ltd.*(1), in which the learned Chief Judge of the High Court, Bombay remarked that "it makes no difference if there is any change in the person who carries on the business as long as the business is continued." The following English cases may also be quoted:—(a) *Rhyope Coal Co. v. Foyer*(2), in which it was held that the conversion of a private partnership into a Company with limited liability created a 'succession'. (b) *Bartlett v. Commissioner of Land Revenue*(3), in which it was held that where a business is sold by an individual to a Company, there is no discontinuance, but a succession, and (c) *Thomson and Balfour v. Le Page*(4), in which the Lord President remarked:—"I think the word "succession" does cover any case of the transfer of one trader to another of the right to that benefit which arises from connection and reputation." My view therefore is that the case is governed by section 26 of the Act and not by section 25 (3) and that the assessment was correctly made.

* Not printed.

(1) 2 I.T.C. 110.

(3) 7 Tax Cas. 229; (1914) 3 K.B. 686.

(2) 1 Tax Cas. 343.

(4) 8 Tax Cas. 541.

A copy of this draft reference, which was prepared by my predecessor, was sent to the petitioner in accordance with Rule 11 of the Rules framed by the High Court of Judicature at Lahore regarding the procedure to be adopted for hearing of references under section 66 of the Income-tax Act, 1922 with the enquiry whether he had any additions or amendments to suggest. The petitioner's counsel has proposed a verbal addition in para 1 of the draft which has been incorporated in the reference. He further asks that copies of the following should be attached to the reference:—L. Asa Nand, Income-tax Officer, Amritsar's order, dated the 10th January 1925, and of Mr. Pearce, Assistant Commissioner of Income-tax, Eastern Division, dated the 8th April 1925 and of Mr. Mitchell, Commissioner of Income-tax, dated the 22nd May 1925. The copies asked for are accordingly attached.

Bevan Petman, for the Assessee.

Jagan Nath Aggarwal, for the Crown.

JUDGMENT.

This is a reference made by the learned Commissioner of Income-tax in compliance with the order passed by a Division Bench of the High Court under clause (3) of section 66 of the Income-tax Act of 1922. The facts are briefly as below:—

The assessee Lala Nathu Mal and his six sons constituted a joint Hindu family and they carried on a business in dyes at Amritsar and some other places under the name and style of Kalu-Mal-Shori Mal and Company. It was stated that the sons separated from the father on the 19th of April, 1923, and started their own separate business in partnership with three outsiders, leaving Nathu Mal, the sole proprietor of the old business to be carried on under the old name and style. All the account books of the former business remained with Lala Nathu Mal and he retained also to himself the right of realising the outstandings of the old business. Lala Nathu Mal contended that in consequence of the disruption of the family and the partition of the family property the old business was discontinued within the purview of section 25 (3) of the Income-tax Act, but the Income-tax authorities came to the conclusion that the result of the change in the constitution of the family firm was that Lala Nathu Mal succeeded to the family business.

As observed by the learned Commissioner it is common ground that if the assessee's contention is well-founded, the case is governed by section 25 (3). But on the other hand, if the view taken by the Income-tax authorities is correct, the case falls under section 26.

It appears that the Subordinate Income-tax Officers expressed conflicting opinions from time to time in respect of the nature of the change in the old business that resulted from the separation of the sons from the father, but those opinions cannot be taken into consideration in deciding the issue which is before us. It is stated that the father imports dyes as before and sells the same to his sons as their commission agent. Further, it is stated that the sons on partition got cash, stocks of dyes and other property from the father. These facts do not go to show that on the disruption of the family the father ceased to carry on the family business. On the other hand, the facts that all the account books of the firm remained with him, that he continued to carry on the business under the old names and style, and that he retained to himself the right of realising the outstandings of the old firm show that he continued the old business. The legal effect of the disruption of a family is to be determined according to the facts of each case. The assessee's contention that the family firm ceased to exist

because the family disrupted, is untenable because the business of a family can continue in spite of its disruption. The question really is whether the business was discontinued or not in consequence of the breaking up of the family. According to the facts stated above, it was not. We, therefore, hold accordingly. The assessee to pay costs of the Commissioner.

(278) **IN THE HIGH COURT OF JUDICATURE AT LAHORE.**

Before Mr. Justice Zafar Ali and Mr. Justice Addison.

(16th January, 1929)

Nawab Muhammad Akbar Khan

.. Assessee.

v.

The Commissioner of Income-tax, Punjab and N. W.
Frontier Province.

.. Referring Officer.

Income-tax Act (XI of 1922), Sec. 9 (2)—House in local Notified area—Annual value, meaning of—If includes house-tax realised from tenant.

The expression 'annual value' in Sec. 9 (2) of the Income-tax Act includes the house-tax payable to the local Notified Area Committee realised by the landlord from the tenant.

Case (Referred Case No. 39 of 1927) stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Punjab, and N. W. Frontier Province for the opinion of the High Court.

CASE.

In an application dated the 6th April 1927, I was asked by the petitioner, who owns extensive house property in Hoti Mardan (N. W. F. Province), to refer a number of questions to the High Court under section 66 (2) of the Income-tax Act. By my two orders dated the 21st June and the 18th July, I declined to refer all the questions except two. One of the latter has since been conceded. The other is the subject of the present reference and, in agreement with the petitioner's counsel, is framed thus:—Does the expression "annual value" as defined in section 9 (2) of the Income-tax Act (XI of 1922) include house-tax, when the latter is payable to the local Notified Area Committee, but is realised from the tenant?

2. In letting his property, it is the petitioner's practice to arrange with his tenants that they should pay him so much on account of rent and so much more on account of house-tax and scavengers' tax, which are payable to the local Notified Area Committee. The petitioner contends that, in determining the annual value of his property for income-tax purposes, both taxes should be excluded from consideration.

3. It is common ground that the case is governed by the construction to be placed upon the definition of 'annual value' given in section 9 (2) of the Income-tax Act. This definition runs as follows:—"For the purposes of this section the expression "Annual value" shall be deemed to mean the sum for which the property might reasonably be expected to let from year to year". It is also common ground that the house-tax is payable by the owner and the scavengers' tax by the tenant. I have conceded the claim that the latter should not be

considered in determining 'annual value', for, though it is paid to the owner, this is done by special arrangement and it is clearly paid to him in a fiduciary capacity for payment to the Committee on the tenant's behalf, and as such it is no part of 'the sum for which the property might reasonably be expected to let'.

4. The position in regard to the house-tax is different. In this case, the liability for payment to the Committee rests upon the owner and the tenant is in no way concerned. Any payment received by the owner is, therefore, 'as much received by him as the amount received on account of what he calls "rent"'. Counsel admitted that, so far as the tenant was concerned, 'the sum for which the property might reasonably be expected to let' included the sum payable by him to the owner on account of taxes, but contended that, so far as the owner was concerned, it included only the sum receivable as 'rent'. In this view I cannot agree, for the expression 'annual value' as defined in the Act connotes a notional value to be determined by 'the sum for which the property might reasonably be expected to let from year to year'; and in my opinion the plain meaning of these words is that it is to be determined by the gross sum that an owner is likely to receive from year to year for the temporary use of his property by a tenant. Not the whole of this sum is assessable, for sub-section (1) of section 9 allows certain deductions; but only these deductions are admissible, and as a house-tax payable to a local body is admittedly not one of them, it cannot, I submit, be excluded from the calculation of 'annual value'. I would, therefore, answer the question in the affirmative.

Badri Das, for the Assessee.

Jagan Nath Aggarwal, for the Crown.

JUDGMENT.

The view taken by the Commissioner of Income-tax is in our opinion correct. Annual value of a house is the sum for which the property might reasonably be expected to let from year to year. Here the tenants are paying what has been assessed as the annual value, and that is the sum for which the property might reasonably be expected to let from year to year. We would, therefore, answer the question referred in the affirmative. We make no order as to costs.

(279) IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Mr. Justice Zafar Ali and Mr. Justice Addison.

(16th January, 1929).

Rai Sahib Lala Jinda Ram

Assessee.

v.

The Commissioner of Income-tax, Punjab and N. W
Frontier Province.

Income-tax Act (XI of 1922), Sec. 2 (4)—Investment of money in company shares—Business, if constituted—Res judicata, applicability of.

Investment of money from time to time in shares of various companies is not business within the purview of the Income-tax Act and a decision to the con-

trary in a prior year will not estop the Income-tax Officer from holding otherwise next year.

Application (Case No. 256 of 1928), under Sec. 66 (3) of the Income-tax Act (XI of 1922) for an order to direct the Commissioner of Income-tax, Punjab, & N. W. Frontier Province to state a case for the opinion of the High Court.

J. L. Kapur, for the Assessee.

Jagan Nath Aggarwal, for the Crown.

JUDGMENT.

The fact of investing money from time to time in the shares of various companies is not business within the purview of the Income-tax Act, and if it was held to be business by an Income-tax Officer once, he or his successor in office, is not estopped from holding otherwise next year.

No question of law arises in this case and we dismiss this application. We make no order as to costs.

(280) IN THE COURT OF THE JUDICIAL COMMISSIONER, NAGPUR.

Before Mr. Findlay, Judicial Commissioner and Mr. Staples

Additional Judicial Commissioner.

[17th January, 1929.]

Dr. Sir H. S. Gour, Bar-at-Law

.. Assessee.

v.

The Commissioner of Income-tax, Central Provinces and Berar.

.. Referring Officer.

Income-tax Act (XI of 1922), Sec. 4 (3) (vii)—Money received by lawyer by sale of legal treatise—If casual income—Unclosed accounts—Sale of books during period of years—Profits therefrom, if assessable as income of account year.

The assessee, a practising lawyer and author of well-known legal treatises, received in the account year 1925-26 a sum of Rs. 11,150 for outright sale of the 3rd edition of his treatise on Penal Law of India. On an assessment for the year 1926-27 of this sum as well as a sum of Rs. 17,600 being the estimated income from the assessee's book Hindu Code from the time of its publication in January 1923 to 31st March 1926, the assessee contended that the former was casual income not assessable and that the latter was assessable only to the extent of Rs. 2,800, being the estimated income from that book during the previous year 1925-26.

HELD, (1) that the income from the sale of the Penal Law of India was neither a capital receipt, nor casual income exempt from assessment under Sec. 4 (3) (vii) of the Income-tax Act,

(2) that the assessment of lump profits made in several previous years in an unclosed account was not legal and that the sum of Rs. 2,800 being the estimated income during the previous year alone was assessable.

Case [Misc. Judicial Case No. 34 of 1927] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Central Provinces and Berar for the opinion of the Court.

CASE.

Under section 66 (2) of the Indian Income-tax Act, 1922, I have the honour to refer the following two points of law arising out of the case of Dr. Sir Harisingh Gour, Kt., M.L.A., Bar-at-Law, Nagpur, for the decision of the Hon'ble Judges of the High Court:—

- (1) Is the sum of Rs. 11,150 received by the assessee on the outright sale of the third edition of his work on the Penal Law of India such income as is liable to income-tax?
- (2) Whether the Income-tax Officer was right in including in his estimate of the assessee's income for the financial year 1925-26 as a basis for his assessment of his income of the year 1926-27, the sum of Rs. 17,600 which is his estimated income for the assessee's work on Hindu Code from the time of its publication in January 1923 to the 31st March 1926, i.e., for the aggregate period of $3\frac{1}{4}$ years or only Rs. 2,800 being his estimate of the income from that book for the "previous year" i.e., the financial year 1925-26?

2. Dr. Sir Harisingh Gour's account year ends with March. For assessment during the year 1926-27 he returned his income of the previous year, i.e., for the year ending in March 1926 at Rs. 36,303. The Income-tax Officer, among other items, added the following to his professional income as they were omitted in the return:—

- (i) Rs. 15,000 out of the fees of Rs. 45,000 received from V. M. Abdur Rahman of Rangoon.
- (ii) Rs. 2,000 out of the fees of Rs. 5,000 received from Mohansingh of Amritsar.
- (iii) Rs. 4,750 out of the fees of Rs. 6,750 received from Jamal Brothers of Rangoon.
- (iv) Rs. 20,000 for general omissions.

The Income-tax Officer found that Dr. Sir Harisingh Gour had not shown any income from his law publications or University examination fees and had to question him on the subject. Dr. Sir Harisingh Gour said that he received from Messrs. Butterworth & Co., for the outright sale of his Penal Code Rs. 11,150 about September-October 1925. He claimed that this was not a taxable income. He also admitted that Messrs. Butterworth had published his Hindu Code and were selling it on his account charging 33 per cent. commission. He admitted that of the 2,500 copies published, only 600 were left and the rest had been sold. He produced no accounts saying he had no accounts of the cost of publication. He wished profits to be calculated at only Rs. 4 per copy on the sales of 60 to 70 copies per quarter. Even then he urged that this income was a "casual gain" and therefore not taxable. As no accounts were produced and as accounts were not stated to have been adjusted year by year and no income from this source was ever returned in the past, the Income-tax Officer treated these as "running accounts" and for reasons given in paragraph 7 of his assessment order, dated the 1st December 1926, calculated the income to be Rs. 17,600, i.e., at Rs. 10 per copy on 1760 copies sold.

3. I now proceed to give my opinion on the points in question:—

Point (1):—Dr. Sir Harisingh Gour claims that income derived from "The Penal Law" is a capital receipt or casual gain and is exempt under section 4 (3) (vii) of the Income-tax Act. Casual or non-recurring receipts are exempt under the sub-section quoted only if they do not arise from business or from the exercise of a profession or vocation. Sir Harisingh Gour is a lawyer. He has written no

less than three law books called "The Penal Code", "The Hindu Code" and "The Law of Transfer in British India". He has thus made writing of law books his vocation and income arising from that vocation is not exempt irrespective of whether it is of a casual or a non-recurring nature, which I do not think these receipts can be said to be. Nor do they appear to me to be "capital receipts".

Point (2) :—It was not the intention of the Income-tax Officer to assess 3¼ years' income at one time. The assessee has not proved either what income he received from the source in question or when he received it. Had he done so, the Income-tax Officer would have included the income of the previous year in the assessment under consideration and taken action under section 34 of the Act in respect of income that escaped assessment in the penultimate year, as he actually did as regards certain other items. From the statement made by Dr. Sir Harisingh Gour on the 26th November 1926, on this point, the Income-tax Officer understood (and I venture to say, correctly; he had good grounds for doing so), that the accounts of Dr. Sir Harisingh Gour with Messrs. Butterworth & Co., were not settled. He had stated: "I have no account of the cost of publication * * * * *". It is true that in June 1927 in connection with his application under section 33 of the Income-tax Act, in this very case, he gave somewhat detailed accounts of expenses and income from this work but he was not entitled to let in at that stage evidence that he showed and should have produced before the Income-tax Officer. All that the Income-tax Officer knew was that approximately a certain number of books had been sold by the end of the previous year. Since no income on this account had been returned in earlier years and since there was no evidence that any of it had accrued or arisen in earlier years he was justified, I submit, in treating it as income of the previous year. I, therefore, submit that this question also should be answered in the affirmative.

W. R. Puranick and A. D. Mande, for the Assessee.

D. N. Choudhari, for the Crown.

JUDGMENT.

1. The present is a reference made by the Commissioner of Income-tax, Central Provinces and Berar, with reference to two points arising out of the assessment of Dr. Sir Harisingh Gour, Bar-at-Law, to income-tax with regard to his income during the year 1926-27. The first point referred to us is whether a sum of Rs. 11,150 received by the assessee for the outright sale of the third edition of his treatise on the Penal Law of India is liable to income-tax or not. Before the Income-tax Commissioner the case of the assessee was that the said amount was either a capital receipt or a casual gain, in neither case liable to income-tax. No attempt was made in this Court to support the position that the amount in question could be considered as a capital receipt, but it was urged that the amount in question fell under the category enunciated in section 4, sub-section (3) (vii) of the Income-tax Act. In order to obtain exemption as casual profits, two conditions have to be fulfilled:—(i) the profits in question must not be the proceeds of a profession, vocation or occupation, or arise from business; and (ii) they must not be annual. We have been referred to the fact that, at page 91 of the Income-tax Manual, express mention is made of the fact that profits derived by an author from his book are taxable. This is, however, after all, only an executive instruction and would not necessarily be binding on this Court. No valid argument has, however, been put forward in favour of the view that the profits in question can fall under the heading of casual receipts. A peculiarly direct connection arises in the case of the assessee between his legal qualifications combined with the exercise of his profession as a lawyer and his authorship of a legal book like the Penal Law of India. It seems to us that the writing of such a book is intimately connected with the exercise of his profession. In the case of the

assessee, he has written at least two other well-known legal treatises and it would appear that his authorship in this connection is a direct source of gain to him. Had the assessee, for example, been a grocer and written a novel dealing with scenes and subjects far removed from and having no connection with, the exercise of his trade, we could imagine that some difficulty might arise in deciding whether profits made from such a novel were casual or not, unless there was definite proof that annual profits were made therefrom over a term of years. In the present instance, no such difficulty arises and the connection between the assessee's profession and his authorship is peculiarly close and direct. Instead of receiving profits over a term of years from the book in question, he has chosen the course of making an outright sale of the edition in question. In these circumstances, we are wholly unable to find that the profits in question are exempt from taxation under section 4 (3) (vii) of the Income-tax Act and we answer the first question referred to us in the affirmative.

2. The second question reads as follows:—“Whether the Income-tax Officer was right in including in his estimate of the assessee's income for the financial year 1925-26 as a basis for his assessment of his income of the year 1926-27, the sum of Rs. 17,600 which is his estimated income for the assessee's work on Hindu Code from the time of its publication in January 1923 to the 31st March 1926, i.e., for the aggregate period of $3\frac{1}{4}$ years or only Rs. 2,800 being his estimate of the income from that book for the 'previous year', i.e., the financial year 1925-26”? The statement of the case by the Income-tax Commissioner on point 2 shows the method in which an amount of Rs. 1,7600 has been taken as the assessment with reference to the Hindu Code. The Income-tax Officer held that, from 1923 upto the end of October 1926, 1760 copies of the book had been sold and he assessed the profits thereon at Rs. 10 per copy. Even if we assume that the assessee had failed in previous years to reveal his profits, if any, or had suppressed them, we know of no authority for the method in which the income-tax authorities have assessed the lump profits made in several previous years. The said method of assessment goes directly in contravention of section 3 of the Income-tax Act.

3. In this Court an attempt was made to urge that what had been done was to assess the profits on a continuous and now finally closed account. In this connection it has been pointed out that the assessee stated that the edition in question was now out of date, but, even so, that does not imply that the remaining copies are unsaleable. They would probably command at least a reduced price and we are wholly unable to agree that here we are dealing with a continuous and now finally closed account. The contention, indeed, taken up on behalf of the Income-tax Commissioner in this Court to the effect that this is now a finally closed account is diametrically opposed to the position taken up by the Income-tax Officer in his order of 1-12-1926, in which he explicitly treated the account as a continuous but unclosed account. The principles laid down in *Commissioner of Income-tax v. Bansilal Abirchand*(1), therefore, apply *proprio vigore* to the present question and we are of opinion that the Income-tax Officer was only at liberty to assess the profits made from the Hindu Code in the year 1925-26; he had the choice, moreover, of treating the account as a continuous and unclosed one, in which event the total profits could be assessed to income-tax when the account was closed. If the income-tax authorities had reason to suppose that the assessee had failed to reveal profits made in any previous year, they had available the remedy laid down in section 34 of the Income-tax Act. We are wholly unable, however, to understand on what legal ground the Income-tax Officer proceeded to tax the assumed income spread over a term of years in an unclosed account in the way he did. As we have pointed out, he had two other remedies

(1) 3 I. T. C. 57.

available, but failed to make use of either. On the second point referred to us, therefore, we hold that the Income-tax Officer was wrong in making the assessment in the way he did and that he was only entitled to assess income-tax on a sum of Rs. 2,800 being the assessee's estimated income from the book in question during the year 1925-26.

4. As either party has partially succeeded and failed in this reference, we make no order as to costs.

(281) IN THE COURT OF THE JUDICIAL COMMISSIONER, NAGPUR.

Before Mr. Findlay, Judicial Commissioner and Mr. Staples

Additional Judicial Commissioner.

[17th January, 1929.]

Dr. Sir H. S. Gour, Bar-at-Law

.. Assessee.

v.

The Commissioner of Income-tax, Central Provinces and Berar.

.. Referring Officer.

Income-tax Act (XI of 1922), Secs. 12 & 23—University Examiner's fees, assessability of—Omission of large amounts in assessee's return—Addition of lump sum by Income-tax Officer in estimating income—Legality.

Fees received by a lawyer as University Examiner's Fees are "income from other sources" assessable under Sec. 12 of the Income-tax Act.

Where the assessee was found to have omitted to include in his return large amounts and the Income-tax Officer in estimating the income added a sum of Rs. 20,000 as for general omissions.

HELD, that there being sufficient matter on record to justify the Income-tax authorities in treating the assessee's return as unreliable, the discretion exercised by the Income-tax Officer in estimating the income was not unreasonable, much less an illegal one.

Case (Misc. Judicial Case No. 35 of 1928), stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Central Provinces and Berar for the opinion of the Court.

CASE.

Dr. Sir Hari Singh Gour, Barrister-at-Law of Nagpur, (hereinafter called the assessee) under section 22 (2) of the Income-tax Act returned the following income for assessment in 1927-28:—

			Income.	Tax paid at source
2. Interest	...	...	2,525	236-11
4. House property	...	...	1,214	
6. Profession	...	...	23,985	
7. Dividends	...	...	13,187	not shown.
			<hr/>	
	Total	...	50,911	

The gross income from profession was stated to be Rs. 39,025; but only net income was shown as an expenditure of Rs. 5,040 was claimed out of it, as:—

	Rs.
Books purchased ..	1,200
Maintenance of a motor car at Rs. 150 per mensem ..	1,800
Salary of a munshi, a clerk and typist at Rs. 105 per mensem ..	1,200
Office rent at Rs. 50 per mensem ..	600
One Chaprasi at Rs. 15 per mensem ..	180
	<hr/>
	5,040

Lists of clients from whom fees (Rs. 39,025) were realised and of companies from whom dividends (Rs. 13,187) were received, were also filed.

2. On comparing these lists with the information collected departmentally, the Income-tax Officer found that at least the following main items had been omitted from them:—

- (i) Rs. 1,450 fees received from R. B. D. Laxminarayan in a Miscellaneous case (Election petition).
- (ii) Rs. 100 interest received on Madras Municipal debentures.
- (iii) Rs. 10,128-2-0 (net) received as dividends from the Tata Iron & Steel Co., Ltd.
- (iv) Rs. 750 dividends from Zehriah Coal Co.

The Income-tax Officer further found that the assessee had not accounted for Rs. 156-8-0 received by him as examination fees from the Patna University, nor made any mention of the income he made on his editions of the Hindu Code and the Indian Penal Law. He therefore did not accept the return; but issued a notice under section 23 (2) of the Income-tax Act.

3. The assessee finally admitted the receipt of items (ii), (iii) and (iv) and of only Rs. 750 as regards item (i). He also admitted the receipt of Rs. 156-8-0 as examination fees but said it was not taxable. He further stated that he sold only 10 or 12 copies of the Hindu Code worth Rs. 300 and in all made a net income of Rs. 19,000 on Penal Law of which a portion was collected in previous year. He said it was troublesome to file list of books purchased for which he claimed a deduction of Rs. 1,200 from his professional income.

4. The Income-tax Officer had letters from the publishers (Messrs. Butterworth & Co.), to show that the assessee was paid Rs. 3,075-11-0 as his share (i.e., two-thirds) on the sale of the Hindu Code which meant that 156 copies of it were sold in the year. As no accounts were produced by the assessee the net income was calculated at Rs. 10 per copy like last year. The Penal Law was sold outright to Messrs. Butterworth & Co., for Rs. 25,000. Of this Rs. 11,150 was taxed last year. Rs. 13,850 were taken this year. The assessee admitted a net profit of Rs. 19,000 and promised to produce his accounts, which he never did. Thus the assessment was made on the following income, (vide Income-tax Officer's order, dated the 10th March, 1928—Ex. A.*) :—

Profession ...	37,365	(Rs. 39,025 minus Rs. 1,200 pay of clerks and Rs. 400 interest).
	1,450	Unaccounted part of the fee from R. B. D. Laxminarayan.
	156/8	University fee
	1,560	Hindu Code
	13,850	Penal Law
	20,000	General omissions
	<hr/>	
	74,381/8	

* Not printed.

House property	1,464	and not 1,214, returned by assessee.
Interest on securities	2,625	
Interest from Bansilal	400	
Dividends gross	26,557/15	
	<hr/>	
	1,05,428	
	<hr/>	

5. Against this assessment, an appeal was filed before the Assistant Commissioner on five grounds, viz. :—

- (i) The Income-tax Officer erred in treating the income earned by the assessee by editing books and University remuneration as assessable income under the law.
- (ii) The Income-tax Officer erred in holding that the assessee made more income than that stated by him from the books edited by him.
- (iii) The Income-tax Officer ought to have accepted the income from profession as stated by the assessee.
- (iv) The Income-tax Officer erred in disallowing the several items of expenditure claimed by the assessee as deductions from professional income.
- (v) The Income-tax Officer ought to have held that the income as returned by the assessee was proper and that he was not assessable for more than the same.

The Assistant Commissioner, (vide his order, dated the 30th April 1928, copy enclosed—Ex. B.*) reduced the taxed income by Rs. 1,130 (i.e., allowed Rs. 180 as peon's pay and Rs. 950 in the fee from R. B. D. Laxminarayan holding that Rs. 750 admitted by the assessee be taken as receipt and not Rs. 1,700).

6. The assessee has now put in an application (copy enclosed—Ex. C.*) requesting that the following points be referred to the High Court:—

- (1) Whether income from books and the University can be classed as "Professional" income within the meaning of law.
- (2) Whether the Income-tax Officer was justified in adding the sum of Rs. 20,000 to the petitioner's income for the purpose of assessment.
- (3) Whether the Income-tax Officer was justified in assessing the petitioner on the following items:—(i) Assessing the rent of the house at Rs. 2,400 per annum when it was assessed by the Municipality at Rs. 1,800 per annum. (ii) Disallowing the cost of a motor car and of the renewal of books. (iii) Disallowing the cost of preparing the MSS of law books for the press.

And generally in not making allowances and deductions claimed by your petitioner.

7. I have to report on each of these points as follows:—

Point (1). It is not denied by the assessee that he has been the author of not less than three books on law, i.e., Law of Transfer of Property in British

India, The Indian Penal Law and The Hindu Code. He has not only written these books once, but has been bringing them upto date also. It is also not denied, that he has been appointed an Examiner in Law by many of the Indian Universities. By writing books therefore the assessee had been exercising the vocation of an author. Similarly it may be said that the fees which he gets from the Universities are derived from his vocation of an Examiner. The phrase "Professional earnings" is not defined in the Act. Under section 11, it is only said: "The tax shall be payable by an assessee under the head 'Professional earnings' in respect of the profits or gains of any profession or vocation followed by him," and the income taxed under this section is shown under side-head 5 of the assessment form I.T. 15. Therefore though the income in brief is shown as income derived from "Profession", it includes all kinds of income that are contemplated under section 11 of the Indian Income-tax Act. The income from editing books, i.e., the income of an author, is taxable, vide Income-tax Manual, page 91 and also Law of Income-tax by Sundaram, page 307.

On the 22nd June 1928, the assessee sent a further note explaining as to what he really meant by questions raised in points (1) and (3). A copy of this application is also enclosed (Ex. D.*). In this letter the assessee seems to contend that the incomes derived from books and the University examinations are casual incomes and therefore not taxable. As regards this I would refer to the provisions made under section 4 (3) (vii) under which only casual incomes are exempt from taxation. This sub-section says that the Act shall not apply to the following classes of incomes, i.e., "Any receipts not being receipts arising from business or the exercise of a profession, vocation or occupation, which are of a casual and non-recurring nature and are not by way of addition to the remuneration of an employee." Now as stated in the last year's reference case also, it is a fact that the assessee is a lawyer. He has made writing of law books his vocation and income arising from it is not exempt irrespective of whether it is of a casual or non-recurring nature, which I do not think these receipts can be said to be. Nor do they appear to me to be capital receipts as the assessee last year contended. My opinion, therefore, is that the income from books and the Universities is correctly classified as professional income and is not exempt. Even if it is held that it is not "Professional earnings", then too it cannot escape assessment. For no income is exempt from taxation unless specifically provided for in the Act, and income which does not fall under any of the first five heads mentioned in section 6, falls under head "(vi) Other Sources", and is taxable under section 12 of the Act: and mis-classification of incomes does not vitiate the assessment made.

Point (2). To understand this question fully it would not be out of place to make reference to the assessments on this assessee in the past. Even the very first return made in 1918-19 was not correct and then the assessee undertook to furnish "an accurate account down to the last anna". This has not been adhered to. Even the return made for assessment during the year 1926-27 disclosed that he did not account for the receipts of as much as Rs. 21,750 from only three clients; but when his attention was drawn to these omissions he began to explain by saying "I do not know that sums paid out of professional fees to middle (men) as their commission are not admissible as deductions and I therefore do not consider it necessary to show the fees that I did not receive for myself. Moreover the payments were a necessary expenditure of the profession. There was no concealment of any part of my income." The return under reference also was found to be very incomplete and incorrect; and the omissions which are noted above amounted to Rs. 15,410 from editing law books, Rs. 10,880-15-0 from dividends, Rs. 100 as interest from debentures and Rs. 500 from professional fees.

* Not printed.

These were only a few omissions that were detected. There may be others that may not have come to light. The explanation of the particularly flagrant omission of Rs. 10,880-15-0 under dividends (which if undetected would have meant that the assessee would have evaded paying super-tax on that amount) can only be described as absurd. It is difficult to believe that the assessee—whose eminence in his profession however your Lordships are better able to appraise than I—ever seriously believed that he was justified in setting off what he calls a “loss” in respect of the capital alleged to have been lost in the shares of the Agricultural Implements Co., Ltd., in 1925 against this item of receipt. The Act does not admit of the principle of setting off taxable income against losses of capital. The assessee must also know perfectly well that even if he had incurred a loss in 1925 he could not set it off against his income of 1926-27. If the assessee honestly claimed any deduction from his actual income, it was his duty imposed by rule having the force of law (Note 5 (b) in the form of Return—Rule 19) to set out his gross income and the deductions claimed in his return, not to make a surreptitious deduction in this underhand manner. I am constrained to say that in view of the assessee’s past conduct and of his behaviour in regard to this item alone, the Income-tax Officer would have been fully justified in imposing a penalty under section 28 (1) for deliberate concealment of income, or in moving the Assistant Commissioner to sanction his prosecution. The assessee never produces his accounts. He contends he keeps none. He alleges that even his deposits he has removed from British India to Ceylon. He does not produce the pass books of the Ceylon banks to enable us to see if any interest has been received in India. In fact the Department is kept in the dark so far as assessee’s accounts are concerned. Looking to all these facts and having regard to the assessee’s past history the Income-tax Officer added Rs. 20,000 for general omissions observing: “The large omissions enumerated above, part 2 tabular form, compel the inference that the assessee more probably than not had several other items of income which he had not disclosed. It is therefore fair to add an estimated sum of Rs. 20,000 more on account of such income to the income already found above.”

In his arguments before me the assessee cited two cases of the Punjab High Court; (i) *Baij Nath v. The Commissioner of Income-tax, Punjab* (1), and (ii) *Messrs. Dhuni Chand Dhani Ram v. The Commissioner of Income-tax, Punjab* (2), and urged that there ought to have been some basis for the Income-tax Officer’s estimate of Rs. 20,000 and that a bare statement of the Income-tax Officer’s estimate was a mere guess without any obvious basis.

The Department too, if left to itself, would have depended upon these rulings. In *Baij Nath v. Commissioner of Income-tax, Punjab* (1), it is held: “Should he (Income-tax Officer) however find on good evidence that even one substantial item is missing, he would be entitled to treat the whole account as unreliable.” In the present case not one but many substantial items are found missing; and the Income-tax Officer is justified in treating the accounts (as produced) as wholly unreliable. All that the other ruling seems to require is that the estimate should have some basis. From the history of the case as given in brief above, and from the omissions detected and totalling to over Rs. 26,000, I think the Income-tax Officer had basis to frame the estimate of Rs. 20,000 and even more for such omissions. I am of opinion that point (?) also should be answered in the affirmative.

I may mention here that the assessee also urged that the omission detected under head “Professional earnings” amounted to only Rs. 700 whereas Rs. 20,000 are added under that “Head” which estimate was very high. In the first place this objection cannot be raised as that is not the objection taken

in this question. In the second place, the estimate is for general omissions, i.e., under other "Heads" also though for brevity's sake it is put down under "Profession" which is the chief source of income of the assessee.

Point (3). This to me seems to be a very general question and a kind of second appeal to the High Court. It is not shown to me as to how this can be called a question of law. I regret I am unable to refer this question for the decision of the Honourable Judges of the High Court, though for their information I note in brief on each of the items supposed to have been disallowed by the Income-tax Officer:—

(i) Under section 9 an assessee is taxed under head "Property" in respect of the *bona fide* annual value of the property consisting of any buildings or lands appurtenant thereto of which he is the owner, What is the *bona fide* annual value of the property is a question of fact and as regards this the Income-tax authorities are sole judges. By comparison with other bungalow property in the neighbourhood it has been found that the bungalow occupied by the assessee has the *bona fide* annual value of more than Rs. 3,000. Hence the Income-tax Officer adopted it. There is no evidence on record to show that the Municipality has valued it at Rs. 1,800 per annum.

(ii) As regards the expenditure of Rs. 1,800 on motor car it is held that the car is not required for profession but for prestige and personal comforts of the assessee.

(iii) Rs. 1,200 were claimed for the old editions of the law books being replaced by new ones purchased; but list of them was wanted and was not produced. For want of evidence this expenditure was disallowed; though otherwise also it would have been disallowed as a capital expenditure.

(iv) No evidence was given as regards the cost of preparing Mss. nor was any account of the income made in editing law books, towards which this expenditure was to be debited, produced. Net income only was estimated. Hence this cost could not be allowed.

(v) Rs. 600 were claimed as rent paid for office. Office is held in the bungalow occupied by the assessee and the Income-tax Officer disallowed this as "payment to self". The Income-tax Officer took this into consideration when he took the *bona fide* value of the bungalow at Rs. 1,800 only and not actually Rs. 2,400.

(vi) Rs. 180 pay of a peon. This has been already allowed by the Assistant Commissioner in appeal.

W. R. Puranick and A. D. Mande, for the Assessee.

D. N. Choudhari, for the Crown.

JUDGMENT.

(1) This case is so far connected with the Miscellaneous Judicial Case No. 34 of 1927, in which we have passed orders to-day, but, in the present instance, the questions we have to consider have reference to the assessment to income-tax of Dr. Sir Hari Singh Gour, Bar-at-Law, for the year 1927-28.

(2) In paragraph 6 of the statement of the case prepared by the Income-tax Commissioner, two points only require our decision. The third point has already been settled by a Judge of this Court (the Judicial Commissioner) in his order, dated the 20th of December 1928, in Miscellaneous Judicial Case No. 61 of 1928.*

* Since Reported as 8 I. T. C. 883.

(3) The first point referred is whether income from books and University Examiner's fees can be classed as professional income within the meaning of the law, or whether such income is exempt from taxation. We have already dealt with the question of the income of the assessee from his legal books in the order quoted above and have nothing to add thereto. As regards the question of Examiner's fees received from the University we are also of opinion that such fees are derived from an activity which follows directly from the fact that the assessee is a leading lawyer who exercises the profession in question. Presumably, the exercise of this activity as an Examiner and the receipt of the consequent fees occur regularly and periodically and we do not think that, in those circumstances, the fees in question can possibly be exempted in the manner desired by the assessee. It may be true that it is not obligatory on the assessee as one of his professional duties to set those papers, but, even so, he is obviously employed for the purpose as an expert in the subject, and he is an expert because of his professional qualifications and his distinguished career at the Bar. Clearly, therefore, the fees in question would at least come under the category of income from other sources. We, therefore, answer the first question in the affirmative and hold that the income from the assessee's books and from his Examiner's fees is liable to be taxed as professional income.

(4) The second point referred to us is whether the Income-tax Officer was justified in adding a sum of Rs. 20,000 to the assessee's income for the purpose of assessment. The reasons taken for this course are clearly laid down in the order dated the 10th of March 1928, of the Income-tax Officer, Nagpur, and the matter was further discussed in the appellate order of the Assistant Commissioner of Income-tax, dated the 30th of April 1928, while a convenient summary of the position is to be found in the remarks on point No. 2 in the Commissioner of Income-tax's statement of the case. We are wholly unable, however, to see that any question of law arises in this connection. The argument put forward on behalf of the assessee as regards the addition of Rs. 20,000 made to his estimated income is that the Income-tax authorities have exercised a purely arbitrary discretion in the matter. We have been referred in this connection to cases like *Bishnu Priya Chowdhurani, In re*(1), *Duni Chand-Dhuni Ram v. Commissioner of Income-tax*(2), and *Pandit Pandurang v. Commissioner of Income-tax, Central Provinces*(3), but we do not think any of these cases are peculiarly apposite or on a par with the facts of the present case. Here, we have an assessee who had omitted to include in his returns very large amounts including one of over Rs. 10,000 from dividends—an amount which, by itself, was nearly a third of his professional income returned by him. Had the amount of Rs. 10,880-15-0 acquired from dividends not been discovered by the Income-tax authorities, the assessee would not have had to pay super-tax thereon, and we are wholly unable to accept the position that the assessee was entitled to keep silent as regards such items of income and set them off against losses of capital. There was, in our opinion, ample material on record from which the income-tax authorities were entitled to draw a reasonable inference that, in view of the discoveries made by the Income-tax authorities as to income and profits not returned by the assessee, there were probably various other items which had not been returned and which, in the nature of things, the Department has been unable so far to trace out. There was, in short, sufficient matter on record to justify the Income-tax authorities in treating the returns made by the assessee as unreliable and we are wholly unable to find that, in the circumstances of this case, there is any *prima facie* proof that the discretion exercised by the income-tax authorities in this connection has been an unreasonable, much less an illegal one. No question of law, therefore in our opinion, arises on the second point and we answer it in the affirmative.

(1) 1 I. T. C. 261.

(3) 2 I. T. C. 69.

(2) 2 I. T. C. 188.

(5). As the Income-tax Commissioner has succeeded in the present case, the assessee must bear his costs therein. We fix Rs. 100 as pleader's fees.

(282) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Sir Murray Coutts Trotter, Kt., Chief Justice, Mr. Justice Odgers and Mr. Justice Beasley.

(17th January, 1929).

The Madras Central Urban Bank, Ltd.

.. Assessces.*

v.

The Commissioner of Income-tax, Madras

.. Referring Officer.

Income-tax Act (XI of 1922), Secs. 8 and 60—Madras Central Urban Bank registered under Co-operative Societies Act—Investment in Government Securities—Interest therefrom, assessability of—Claim of exemption as profits of Co-operative Society—Exemption Notification under Sec. 60.

The Madras Central Urban Bank Ltd. incorporated under the Co-operative Societies Act was formed inter alia for financing co-operative societies as the Provincial Apex Bank and carrying on general banking business not repugnant to the provisions of the Co-operative Societies Act. On an assessment of the interest derived from investments in Government Securities under Sec. 8 of the Income-tax Act, the Bank contended that under Government orders to keep 10 per cent of its total call liabilities in liquid form, its fluid assets instead of being kept in a safe were invested in Government Securities and claimed exemption as "the profits of a co-operative society" within the meaning of the Notification issued under Sec. 60 of the Act.

HELD, that the investment of the fluid assets not being part of the business of the Bank, interest therefrom was not 'profits' exempt under the Notification, but 'income' assessable under Sec. 8 of the Act.

Case (O. P. No. 202 of 1928), stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras for the opinion of the High Court.

CASE.

I have the honour to state the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (2) of the Indian Income-tax Act, XI of 1922.

2. The petitioner, The Madras Central Urban Bank, Ltd., hereinafter called the "Society" is a Society incorporated under the Co-operative Societies Act, 1912 (II of 1912). The objects for which the Society was formed are as follows:—(a) to collect funds for financing co-operative Societies, (b) to serve as the Provincial Apex Bank for the province of Madras, and (c) to carry on general business of banking not repugnant to the provisions of the Co-operative Societies Act and the rules framed thereunder for the time being in force.

3. For the assessment of the year 1927-28 the Income-tax Officer, Second Circle, Madras called on the Society under section 22 (2) of the Income-tax Act to make a return of its income. The Society returned an income of Rs. 22,278, under the head "Interest on mortgages, loans, etc.", and stated that the income derived by it from securities already taxed and declared to be income-tax free

had not been shown in the return as it was not liable to income-tax. The Income-tax Officer pointed out that the income so derived by them was liable to super-tax and called on the Society to furnish those particulars. The Society returned an income of Rs. 1,33,110 from tax free securities, Rs. 13,442 from interest on securities taxed at source and Rs. 35,000 income derived from investments in the Bengal Provincial Bank and claimed to deduct therefrom the expenditure incurred by it in earning that income, viz., the interest paid on moneys borrowed by it and utilised for the purchase of securities and investments computed at an average rate of 4.62 per cent. per annum. The Income-tax Officer allowed the claim and computed its total and taxable income as under:—

	Rs.
<i>Securities:—</i>	
Taxed	.. 4,574
Tax free	.. 70,686
<i>Other sources:—</i>	
Investments	.. 22,278
	<hr/>
Total income	.. 97,538
	<hr/>
Deduct income from tax free securities and securities taxed at source	.. 75,260
	<hr/>
Taxable income	.. 22,278
	<hr/>

He levied income-tax and super-tax on this basis.

4. The Society appealed to the Assistant Commissioner and contested its liability to be assessed under the Act on the ground that by a notification issued by the Governor-General in Council under the powers vested in him by section 60 of the Income-tax Act (a copy of which is appended marked Exhibit A), the profits derived by it were exempt from the tax payable under the Income-tax Act. The Assistant Commissioner dismissed the appeal holding that the income derived by the Society from investments and interest on securities did not fall within the exemption.

5. The Society now requires me to state a case and refer for the decision of the High Court the following question:—“Whether the Madras Central Urban Bank is liable to pay income-tax and super-tax in respect of the interest on securities and investments”?

So far as the claim relates to the sum of Rs. 22,278 being interest on a deposit I am prepared to concede that this is a part of the profits of the Society assessable under section 10 of the Income-tax Act and is covered by the notification. I have accordingly eliminated this item from the assessment. As regards the interest on securities however, I am of opinion that such income is taxable under section 8 which enacts “The tax shall be payable by an assessee under the head “Interest on securities” in respect of the interest receivable by him on any security of the Government of India, or of a Local Government, or on debentures or other securities for money issued by or on behalf of a local authority or a company”. The Society claims exemption of the interest on the strength of the notification referred to above. The notification exempts the “profits” of any Co-operative Society from the tax payable under the Income-tax Act, and unless the interest can be brought within the express terms of that notification it is not entitled to the exemption sought for. On an examination of the language employed in the Income-tax Act it seems to me that the words “income” and “profits and gains” have been used in the Act to denote distinct

subject matters of taxation; for example, the word "income" is used with reference to "salaries", "interest on securities" and "property" and the words "profits and gains" with reference to "Business" and "Profession". The term "profits" used in the Notification is never applied to "interest on securities" which is consistently termed "income", and in my opinion an exemption in respect of "profits" cannot apply to that which the Act does not term "profits".

The history of the notification also makes this position clear. The first notification exempting the profits of Co-operative Societies is that of the Government of India, No. 6216, S.R., dated 30th September 1904, re-published on page 1106 of Part I of the Fort St. George Gazette, dated 18th October 1904, which declared that "the profits of any Co-operative Society for the time being registered under the Co-operative Societies Act (X of 1904), or of dividends or other payments received by the member of any such society on account of profits are exempt from income-tax." After the passing of the Co-operative Societies Act (II of 1912) a similar exemption was granted by the Governor-General in Council in the Notification of Government of India, No. 681-F, dated 28th December 1912, re-published on page 49 of Part I of the Fort St. George Gazette, dated 14th January 1913. These notifications were issued at a time when the Income-tax Act II of 1886 was in force. Interest on securities was then a distinct subject of taxation and was assessed under the second schedule to that Act—Part III. At that time doubts were expressed as to whether the notification exempted from income-tax the interest on securities held by Co-operative Credit Societies and the Government of India explained their intention and stated that the exemption applied only to the profits and gains made by such societies and that income-tax should be levied under Part III of the second schedule of the Income-tax Act, 1886, on the interest of all securities held by them. A copy of the Government of India's letter on the subject is appended (Exhibit B.*). Subsequent practice has consistently followed the instructions therein issued. The present Notification is merely a reproduction of the old and in the absence of any indication to the contrary should, it appears to me, be construed in the light of its origin as explained above.

I am accordingly of opinion that the interest on all securities held by the petitioner Society is liable to income-tax and super-tax.

NOTIFICATION.

INCOME-TAX.

Simla, the 25th August, 1925.

R. Dis. No. 291-I.T./25.—In exercise of the powers conferred by Section 60 of the Indian Income-tax Act, 1922 (XI of 1922), and in supersession of the Notifications of the Government of India in the Finance Department No. 681-F, dated the 28th December 1912 and No. 718-F, dated the 8th March 1922, the Governor-General in Council is pleased to direct that the following class of income shall be exempt from the tax payable under the said Act, namely:—

"The profits of any Co-operative Society other than the Sanikatta Salt-owners' Society in the Bombay Presidency for the time being registered under the Co-operative Societies Act, 1912 (II of 1912), or the dividends or other payments received by the members of any such Society on account of profits".

A. TOTTENHAM,

Joint Secy. to the Govt. of India.

M. Subbaraya Ayyar, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

This is a case stated for our opinion by the Commissioner of Income-tax at the request of the Madras Central Urban Bank, Ltd., This is a society registered under Act II of 1912, and the question arises from its assessment on interest derived by it from investments in Government securities. The society contends that it is exempted from paying tax in respect of these investments by a notification in the Finance Department issued under section 60 of the Indian Income-tax Act, 1922 which corresponds to section 28 of the Co-operative Societies Act enabling the Governor-General in Council to remit income-tax payable in respect of the profits of the society. The question is whether this interest is part of the profits of the society.

The notification Ex. A exempts "the profits of any Co-operative Society registered under the Co-operative Societies Act, 1912, or the dividends or other payments received by the members of any such Society on account of profits". The notification has been interpreted not to include interest on securities which according to the Commissioner is consistently termed "income". "Profits" according to him does not include interest on securities and hence the latter is taxable. The contention for the Bank is that it is bound by the Government orders to keep 40 per cent. of its total liability under call deposits in a liquid or fluid form and that, instead of keeping these fluid assets in their safe or till, they keep them in as nearly a fluid form as possible in Government securities upon which, of course, they receive interest. It is said that this is part of the business of the bank and that unless this interest were received the activities of the bank would be very severely handicapped. That of course is a matter for detailed examination of accounts and balance sheets and so on of which nothing has been attempted before us. But what we have to decide is as to whether this investment in Government Securities is part of the business of the bank or whether such investment falls under section 8 of the Act which says "The tax shall be payable by an assessee under the head 'interest on securities' in respect of the interest receivable by him on any security of the Government of India or of a Local Government"; whereas the bank contends that it should be assessed under section 10 (1) "The tax shall be payable by an assessee under the head 'Business' in respect of the profits or gains of any business carried on by him." If the bank is assessed under that head no tax will be payable.

Mr. M. Subbaraya Iyer for the bank has referred us to several English cases. Before referring to them, however, it may be as well to note that the English Income-tax Act, 1918 is a good deal more complicated than the Indian Act and that the English Statute is divided under Schedules with rules under each Schedule. For instance, Schedule (C) concerns tax charged in respect of profits arising from interest, annuities, dividends and shares of annuities payable out of public revenue; schedule (D) tax charged in respect of profits or gains to any person residing in the United Kingdom (1) from any kind of property whatsoever, (2) from any trade or profession, etc.; so that, really the only question that arises on this reference is, whether the investment is part of the Bank's trade or not; in other words, whether it falls under 1 (3) of their bye-laws, 'to carry on general business of banking not repugnant to the provisions of the Co-operative Societies Act.' Turning to the Indian Act, it will be observed that this complication of Schedules is absent, but the section 6, which is the first section in Ch. III headed "Taxable Income" divides the heads of income which are

chargeable to income-tax into (1) salaries, (2) interest on securities, (3) property, (4) business, (5) professional earnings, and (6) other sources.

To refer to the cases cited by Mr. Subbaroya Iyer: *Smiles v. Australasian Mortgage & Agency Company*(1), a company in the course of wool-broking business granted temporary advances on the security of second mortgages on wool and produce. The Court of Exchequer, Scotland, held that interest was chargeable under the first case of Schedule (D), i.e., trade, manufacture, etc. The Lord President pointed out that the account between the company and its customers was of the nature of a current account as between bankers and customers and held that this was proper trading and nothing else and not investment of money upon securities. Lord Shand said "If a company which has a large rest fund laid aside for the purpose of investment makes investments in foreign stock or other foreign securities, that is a case in which the charge is to be made under the fourth case." But the President was of opinion that the present case was entirely different because the Company was doing the business of wool-brokers. Lord Shand also thought: "It is quite unlike a case of investment; the interest fluctuates; it is for no fixed period; the transaction may be closed at any time. In short it is the case of a wool-broker combining with his business that of a banker." But as Lord Shand further points out: "If this had been the case of a banking company carrying on the business of a bank that would not be a case falling within the fourth case, which is the case applying to investments."

Scottish Investment Trust Company v. Forbes(2), is also a decision of the Court of Exchequer, Scotland. That was a case of an investment company and therefore investment was an essential feature of the business and therefore the net gain made by the Company by realizing investments at higher prices than were paid for by them were to be reckoned among the profits and gains for the purpose of assessment. *Norwich Union Fire Insurance v. Magee*(3), That was an insurance company receiving as part of their profits interest on American securities not remitted to the United Kingdom. Held that the interest formed part of the profits of the company being assessable under case (1) of Schedule (D).

So in *Liverpool and London and Globe Insurance Company v. Bennett*(4), the Liverpool and London and Globe Insurance Company carried on business at home and abroad. By the laws of certain of the foreign countries in which it conducted its business the company was required to deposit with the Governments of those countries certain sums of money and to invest those sums in accordance with the local laws. This was done. They also voluntarily invested certain other sums. Both classes of investments yielded interest which was received abroad and not remitted to the United Kingdom. It was held that the interest on both classes of investments was assessable under the first case of schedule (D) as being part of the business. Hamilton, J., held that the voluntary investments were not for the sake of investments but for the sake of having a fund abroad readily realisable to meet the liabilities of their business and that the making of the investments was just as much part of their mode of conducting the business as the taking of risks and in the event of the current account at the bank being insufficient to meet the liabilities, all the investment funds might have to be called upon at some time or other. The object of the investments was to extend the business, so the making of them was part of the business. These extracts from the judgment of Hamilton, J., seem to me sufficient to at once distinguish this from the case before us. In (1913) App. Cas. 610 this very case went to the House of Lords after having been affirmed by the Court of Appeal in (1912) 2 K.B. 41.

(1) 2 Tax Cas 867.

(3) 3 Tax Cas. 457.

(2) 3 Tax Cas 231.

(4) 6 Tax Cas 827 ; (1911) 3 K. B. 577.

This Lordships dismissed the appeal holding that the income of the foreign investments formed part of the profits or gains of the Company's business and was properly taxed under case 1 of Schedule D. See Lord Loreburn at page 619 who adopts Buckley, L.J.'s, expression that the investments were "the fruit derived from a fund employed and risked" in a business coming within the statutory description. It has also to be noticed that (1913) App. Cases was not a case of Government securities. It seems to me impossible, at least without a great deal more information than has been presented to us, to say that these investments of more or less amounts for a longer or shorter time on the part of the bank in order to prevent their fluid assets from lying absolutely idle in their coffers formed part of the business of the bank. It seems to me that they are in the same position as any private person who with a large credit balance in his private account desires to put it into a remunerative form which shall at the same time be readily realisable and therefore invests for shorter or longer periods in Government paper.

Mr. Patanjali Sastri for the Crown cited *Back v. Daniels*(1), where the Court of Appeal held that under the peculiar circumstances of that case Daniels were occupiers of some part of the land in question which prevented them being assessed under Schedule D, but the importance of the case is in the expression of the opinion of Scrutton, L.J., at page 544, that "when there is a separate and distinct operation unconnected with the occupation of the land, such as a cheese factory dealing with the milk of a dairy farm, or a butcher's shop dealing with the beasts of a cattle farm, I can understand a separate assessment of that operation; but I do not think that the fact that the farmer sells his produce either on the farm or at the local market, or at Mark Lane, or even if he sells it in a shop, justifies an assessment under Schedule D as well as or in substitution for Schedule B."

It therefore seems to me from the best consideration that I can give to the matter that this investment of these fluid assets of the bank cannot be held to be part of the business of the bank in accordance with the decisions quoted from the Scotch and English cases which seem to me to be all distinguishable and to be clearly assignable to an operation in furtherance of the particular business of the firm or company concerned. The obligation on the bank to keep 40 per cent of its total liabilities in a fluid form is in consequence of an administrative order of Government and does not oblige them, although it may permit them, to invest the fund at all and it seems to me that as they are to hold the fund in readiness to meet some particular liability which is specified, it cannot be said to be part of their business as a bank to invest these liquid assets in the interval. I think therefore the decision of the Commissioner was right.

We think the bank must pay Rs. 250 for the Commissioner's costs.

(283) IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Mr. Justice Zafar Ali and Mr. Justice Addison.

(21st January, 1929).

Ram Pratap-Sukh Dial

v.

.. Assessee.*

The Commissioner of Income-tax, Delhi.

Income-tax Act (XI of 1922), Secs. 13, 23 (2) and 31—Appeal to Asst. Commissioner—Disposal without recording reasons—Notice under Sec. 23 (2), if dispensed by Sec. 13.

(1) 9 Tax Cas. 183; (1925) 1 K. B. 526.

• A. I. R. (1930) Lah. 277.

In disposing an appeal the Assistant Commissioner must state facts and give reasons for his findings.

Sec. 13 of the Income-tax Act does not empower an Income-tax Officer to dispense with a notice under Sec. 23 (2).

Application [Civil Misc. Application No. 334 of 1927] under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) for an order to direct the Commissioner of Income-tax Act, Delhi, to state a case.

Jagan Nath Aggarwal, for the Assessee.

Carden Noad, for the Crown.

JUDGMENT.

The two orders in appeal recorded one after the other in this case by the Assistant Commissioner of Income-tax are extremely perfunctory and brief, giving no statement of facts and no reasons for the conclusions arrived at. We are of opinion that the Assistant Commissioner must state facts and give reasons for his findings. The Assistant Commissioner of Income-tax, who does not do so, fails to perform his duty properly. It may further be observed that some remarks in the order of the Income-tax Officer which was appealed from, are not quite intelligible, and it appears that he made an estimate of the income on the general report of the extent of the assessee's business.

But this application under Sec. 66 (3), Income-tax Act appears to be premature in as much as some of the questions raised before us are yet to be enquired into under the order of remand made by the Commissioner who will pass final orders on receiving a return to his order of remand. We may further observe that an Income-tax Officer does not appear to be empowered by Sec. 13 to dispense with a notice under Sec. 23 (2), but it not clear from the papers before us whether a notice under Sec. 23 (2) was served on the assessee or not.

With these remarks we dismiss this application on the ground that it is premature. The assessee will be at liberty to present a fresh application, if so advised, after the Commissioner has passed his final orders. We refrain from expressing any opinion as to whether the questions sent back by him for inquiry are questions of law or not. No order as to costs. The hundred rupees already deposited by the petitioner may be refunded.

(284) IN THE HIGH COURT OF JUDICATURE AT CALCUTTA.

*Before Sir George Rankin, Kt., Chief Justice, Mr. Justice C. C. Ghosh and
Mr. Justice Buckland.*

(1st February, 1929)

Messrs. Harackchand Tolaram

v.

.. Assessee.

The Commissioner of Income-tax, Bengal

.. Referring Officer.

*Income-tax Act (XI of 1922), Sec. 10—Partner borrowing from firm—
Interest thereon, assessability of.*

*Interest paid by a partner of a firm to the firm in respect of a sum of
money lent to him by the firm is assessable as the firm's income.*

Case stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bengal, for the opinion of the High Court.

CASE.

In accordance with the provisions of section 66 (2) of the Income-tax Act (XI of 1922), I have the honour to refer for the decision of the Hon'ble High Court a question of law arising out of the appellate order passed on 10th December 1926 by the Assistant Commissioner of Income-tax, Head-quarters, in connection with the assessment made on the firm of Messrs. Harackchand Tolaram for 1926-27 by the Income-tax Officer, District IV(2), Calcutta.

The facts in this case are as follows:—On the 5th May, 1926 a notice was issued to the assessee calling for a return under section 22 (2), which he submitted on 20th August 1926 showing an income of Rs. 2,422. In compliance with a notice under section 23 (2) the assessee produced accounts on 3rd September 1926, and an assessment under section 23 (3) was made on the result of the examination of these accounts on the 22nd September 1926. At the time of the assessment the assessee claimed that the interest of Rs. 2,426-4-9 received from partners which the Income-tax Officer included in it, should be deducted from the total income, but this was not allowed by the Income-tax Officer.

Against the assessment the assessee filed an appeal before the Assistant Commissioner of Income-tax, Headquarters on the 22nd October, 1926, in which he urged that if interest paid to a partner is not to be treated as an expenditure to be set off against income, interest received from the partner should not be included in the profit. The Assistant Commissioner of Income-tax, however, held that the two cases were quite different, and that the interest received from the partners had been rightly included in the profit of the firm. He rejected the appeal on the 10th December 1926.

On the 10th January 1927, the assessee filed an application before me under section 33-66 (2) for review of Assistant Commissioner's order passed on appeal or in the alternative for reference to the High Court of a question of law arising out of that order. I passed orders on the same day declining to interfere in review, and asked him to state the question in a clearer form.

Two questions of law were accordingly stated by the assessee on the 12th January 1927, which are as follows:—(1) Whether in an unregistered firm, where interest is paid by the firm to a certain partner and interest is received by the firm from certain other partners, such interest is to be reckoned as interest on proprietor's or partner's capital as per note 5 of section 22 (2)? (The assessee here clearly refers to note 5 (b) (iii) to rule 19 of the Income-tax Rules 1922). (2) Whether in an unregistered firm the Income-tax law permits the receipt of interest by the firm from a partner to be treated in law as the firm's profit, when payment of interest by the firm to the partner is not allowed to be deducted as a disbursement under section 10 of the Act?

“Such interest” in the first question evidently means interest paid to a partner. Otherwise the question would be meaningless. But if the question relates to interest paid to a partner it does not arise out of the Assistant Commissioner's appellate order since the assessee did not raise it in appeal. In fact it will be seen from the 2nd ground of appeal and paragraph 5 (a) of the application for a reference to the High Court that the assessee's whole case is that interest paid by the firm to a partner is not “the firm's disbursement” as they put it. I do not therefore refer this question. The second question is somewhat clumsily framed and in fact implies two questions. It is correspondingly diffi-

cult to give a simple answer to it. My answer put as briefly as possible is as follows:—

- (1) Whether interest paid to a partner is to be allowed as a deduction from the firm's profit depends on whether the interest is paid on a legal loan advanced to the firm by the partner in his individual capacity or on capital subscribed for the firm's purposes by the partner in his capacity of partner. (This question does not arise as already stated but it has to be referred to in order to make what follows intelligible).
- (2) The question whether interest paid by a partner to a firm is the firm's income or not is an entirely distinct question. It has no sort of connection with the question whether interest paid to a partner by a firm is an admissible deduction from the firm's income or not. Nor can similar principles be applied to decide the two questions. When interest paid to the partner is concerned the dual capacity of the partner has to be considered. But I am unable to imagine any circumstances in which money could be advanced by the firm to a partner *as partner* on which he could possibly become liable to pay interest *as partner* to the firm.

If money is advanced to a partner by his firm it can only be advanced (1) for the purposes of the firm, or (2) for his private purposes. In the first case there can be no liability to pay interest, for in fact there is no "advance" in the ordinary sense of the term. In the second it is obvious that he is in the same position as any other customer, just as he would be if he bought goods from his firm (as he well might) for his own use. Any income that the firm may derive from transactions in which a partner is in the position of an ordinary customer is obviously the firm's taxable income.

It has not been suggested what it is, if it is not the firm's income, or under what provision of law if it is the firm's income it is exempted from the tax.

Sarat Chundra Basak and Rupendra Coomar Mitter, for the Assessee.

N. N. Sircar (Advocate-General) for the Crown.

JUDGMENT.

RANKIN, C. J.:—In this case the Commissioner of Income-tax, under request of the assessee had stated two questions of law for the opinion of the Court under section 66 (2) of the Income-tax Act of 1922. Upon that case coming on for argument this Court made an order under clause (4) of section 66 by which it pointed out that the questions raised were abstract and in some respects unintelligible and were not questions shown to arise on any findings of fact. In these circumstances the Court was of opinion that it was not possible to answer the questions. The matter was sent back to the Commissioner with a view that he might state the necessary facts drawing the necessary inferences on the facts and leaving the Court in a position to see whether any questions of law and, if so, what arose which could be covered by the questions originally proposed.

It appears that the question which is now pressed is a question which arises only with regard to the second of three accounts which appear in this firm's books. As regards the third account mentioned in the letter of reference the learned Advocate for the assessee states no point and it does not appear to me that in these circumstances it is necessary for this Court to answer any question with reference to account No. 3. Account No. 2 is an account which stands in the name of Harakchand Nathmull. Harakchand was one of three partners who died

before the year of accounting leaving two sons Manmull and Nathmull and this account is in the name of Harakchand Nathmull. In that account it appears that there is a debit of interest of Rs. 1,960-15-0. The present dispute arises with reference to that item. The Income-tax Officer on an analysis of the books and on examination of the accounts produced finds as a fact that this is interest on loans taken from the firm. If it is interest on loans taken from the firm then that interest must be taken into account when computing the firm's profit. It matters nothing for this purpose whether the profit has been made by a transaction between the firm and a stranger or by a transaction between the firm and a partner. To whomsoever the firm lends money on interest, the money for interest when it comes in becomes the firm's property. That however presupposes that the real nature of the transaction was a loan by the firm to a partner. The question of fact is whether upon these thoroughly unscientific and muddled books of account there was evidence from which the Income-tax Officer could find that this debit of interest was what it purported to be—i.e., a debit of interest upon money lent. The Income-tax Officer has given what appear to be very intelligible reasons for holding that the interest debited to this No. 2 account is interest on loans taken from the firm and as such should be regarded as profit of the firm. That is a finding of fact and it is a finding of fact upon evidence. It is not a finding which this Court can disturb on reference. Accordingly it appears to me that the questions which are originally propounded to us being of a character which cannot be answered do not arise out of the facts of this case. It is enough to say that as a matter of law whether interest paid by a partner of a firm to the firm in respect of a sum of money lent to him by the firm is the firm's income is a question which in the circumstances of this case must be answered in the affirmative.

The assessee must pay the costs of this Reference including the costs of the original Reference.

GHOSH, J.:—I agree.

BUCKLAND, J.:—I agree.

(285) IN THE COURT OF THE JUDICIAL COMMISSIONER, NAGPUR.

Before Mr. Mohiuddin and Mr. Staples, Additional Judicial Commissioners.

(1st February, 1929).

Radhakisan Ramnarain

.. Assessee.*

v.

The Commissioner of Income-tax, Central Provinces
and Berar

.. Referring Officer.

Income-tax Act (XI of 1922), Sec. 10—Burden of proof—Claim of loss by assessee—Accounts not showing opening balance—Sufficiency as to proof of loss.

Where income has been admitted the burden of proving loss is upon the assessee who alleges them.

Losses cannot be held to be proved by merely showing figures for purchases and sales during the year without the opening balance on hand at the beginning of the year.

Case [Misc Judicial Case 39-B of 1928] stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, Central Provinces and Berar for the opinion of the Court.

CASE.

In compliance with the orders contained in the Additional Judicial Commissioner's Judgment, dated the 25th June 1928, received in the office on the 16th July 1928, I beg to state the facts of the case for the decision of the Honourable Judges of the High Court as follows:—

2. Raghunathdas Rampratap (owner Radhakisan Laxminarayan of Akola) hereinafter called the assessee, observes the Diwali year for his accounts. For assessment during the year 1925-26, he made a return of his income made during the year ending in Diwali 1924 as:—

	Rs.
Property ..	10,473-12 6
Business. Loss ..	5,034-13-9
Total income ..	<u>5,433-14-9</u>

Along with this return papers were also enclosed on which were jotted down the items of receipt and expenditure. On expenditure side was shown an item of Rs. 24,528-1-9 claimed as loss in cotton business. This return was not accepted as correct and the Income-tax Officer who originally made enquiries into the case, asked for the accounts to be produced in support of the return made. He examined them and, under the orders as then obtaining, submitted his report to the Assistant Commissioner who made assessments in cases of incomes of Rs. 10,000 and over. The Assistant Commissioner heard the assessee, looked into the accounts and made an assessment on an income of Rs. 44,847-6-0, vide his order dated the 17th December 1925, copy enclosed (Ex. A.*). Increase in the total taxed income was due to the disallowance of certain items of expenditure and to the addition of certain incomes not properly accounted for in the return. The loss of Rs. 24,528-1-9 which the assessee claimed in Ruth Gathan Khata was not allowed. He gave the following reasons for it:—"As regards the loss of Rs. 24,528 last year I had only estimated his income and I called for last year's account books to-day to see if any stock was left with him and how he had disposed of. The account is produced which is only a running account in his books of the business carried on under the name of Dongulal Ghisulal and when the books of this were called for, Seth Radhakisan says that he could not find those books. I am therefore unable to take this loss into account for the simple reason that the closing stock and sale proceeds thereof of last year is not shown. I will disallow it and add this loss to the income returned as my information is that assessee made great profit over it and is not at all in loss."

3. Against this assessment an appeal was preferred to the Commissioner on no less than 12 grounds, only the first four of which referred to the item of Rs. 24,528-1-9, the rest to other items. The first four grounds of appeal were:—

- (1) That the learned Assistant Commissioner erred in disallowing the loss in cotton of Rs. 24,528-1-9 when the same was duly proved and verified from account books regularly kept by the assessee from day to day.
- (2) That in the absence of any evidence the learned Assistant Commissioner erred in law in imagining that your petitioner had with

* Not printed.

him in stock bales of cotton of last year and that he made profits over the same and that the loss of Rs. 24,528-1-9 actually incurred in cotton as shown above was set off against imaginary profits made on the stock left.

- (3) That the learned Assistant Commissioner erred in law in using information which might have been collected by him *ex parte* and resting his decision thereon.
- (4) That the learned Assistant Commissioner should have openly examined his informants on oath and given an opportunity to your petitioner to cross-examine them, before their statements could be used as evidence against him.

From these grounds of appeal it appeared that the assessee thought that he had proved the loss of Rs. 24,528 but that the Assistant Commissioner did not admit that loss because of his having some information of which the assessee was not informed, nor was given an opportunity of cross-examining it. In appeal reduction in the total income taxed was made to some extent on account of other items; but no reduction on account of this loss was made as it was held to have been not proved and as the Assistant Commissioner's observation regarding his having information that the assessee made great profit over the cotton business was found to be redundant and not to have biassed his mind in making assessment (vide para 2 of the appellate order dated the 8th July 1926—copy enclosed—Ex. D.*).

4. On the 5th of August 1926 the Assessee put up an application under section 66 (2) of the Income-tax Act, 1922, and asked for as many as 9 points to be referred to the High Court, vide his application, dated the 31st July 1926, (copy enclosed—Ex. C.*). As will be seen from this application all the questions raised were regarding the Commissioner being justified or otherwise in disallowing the loss of Rs. 24,528-1-9. In my order dated the 17th August 1926 (Ex. D.*), refusing to refer the points to the High Court, I reiterated the fact that the loss claimed by the applicant had not been proved as account books in its support were not produced and that it was a mere question of fact and not of law and therefore could not be referred to the High Court.

5. It seems that in the month of February 1927, the assessee presented an application to the High Court under section 66 (3) and as mentioned therein wanted only three points of law as arising out of the facts of the case to be referred to the High Court. These points of law are:—(a) Was the Commissioner of Income-tax right in interpreting the Assistant Commissioner's order to mean that the loss was not proved notwithstanding the facts disclosed by the Assistant Commissioner's order, dated 17-12-1925. (b) was the Commissioner of Income-tax right in interpreting the Assistant Commissioner's order to mean that no imaginary profits from a supposed stock were added in order to set off the loss of Rs. 24,528 sustained by the assessee (c) if not, was not the addition unjustified and bad in law as based on mere suspicion or irregular and hearsay information and in the face of the assessee's statement denying the new and imaginary source of income.

6. The order which the Honourable the Judges of the High Court has issued to me does not disclose the question of law on which the case has to be stated; that is to say, whether they are the 9 questions mentioned in the application, dated the 31st July 1926, presented to me under section 66 (2) or the 3 questions mentioned in the application, dated February 1927, under section 66 (3) to the High Court. I

presume to be the latter. In *Jainarayan Motiram v. Commissioner of Income-tax, Central Provinces*(1), the same learned Judge seems to have held that it is for the Commissioner to frame the questions of law as arise out of the facts of the case and "an assessee is entitled to move the High Court for a direction to the Commissioner to refer questions of law raised by him in his petition to this Court even though they may not have been raised before him in the course of the proceedings under section 66 (2) of the Income-tax Act." In his judgment given in the same case *H. F. Hallifax, A. J. C.*, however observes: "But I am at a loss to see how the Commissioner can refer a question of law to the Court with a statement of the case on it unless it is formulated for him. The Commissioner is apparently aware of this but has courteously done his best by his stating the case on all the points raised in the petition presented to this Court whether of facts or law." This decision does not, therefore, give me any definite guidance on this point. In *Thiruvengada Mudaliar v. The Commissioner of Income-tax, Madras*(2), however the Madras High Court held that: "The only questions here are whether the assessee is bound to raise before the Commissioner in his application to him all questions of law relied upon by him and whether he can get a reference upon a question of law not raised by him before the Commissioner. We are clearly of opinion that he cannot do the latter. Under section 66 (2) of the Income-tax Act the Commissioner may be required by the assessee to refer any question or questions of law arising upon the order. It is, we think, beyond doubt that that can only mean any question of law then raised before the Commissioner, not any question of law which the assessee may deem to be an arguable one thereafter. This view is also taken by the Allahabad High Court in the matter of *Lalla Mal Hardeoas Cotton Spinning Mills*(3) and in the matter of *Makhamlal Ram Sarup*(4). If the point of law is not raised before the Commissioner within the time specified by section 66 (2) it cannot be raised at all and the Commissioner cannot be required to state a case raising that point. This is not an appeal to the High Court. No appeal to the High Court is given by the Act. Questions of law and not of fact may be referred to the High Court but only subject to the provisions of section 66, sub-section 2, which only allows a reference upon such points of law as have been raised before the Commissioner within one month of the passing of the order." I therefore submit that I cannot be asked to state the case on those points of law that were not raised before me in the application made under section 66 (2). However as I have been already ordered to state, I do so subject to the objection stated above.

7. *Facts of the case.* And here I would respectfully venture to give expression to the embarrassment that I experience owing to the fact that the High Court's order appears to decide in anticipation important points bearing on the matters now submitted for their decision. It contains a specific finding that "The conclusion was irresistible that the assessee suffered a loss of Rs. 24,528-1-9 in cotton business of the year 1923-24" (Para 8) and "The inclusion of the item of Rs. 24,528-1-9 on the income side or its exclusion from the debit side of the account or of the return could not be justified" (Para 15). I am none the less justified, I trust, in expressing my own opinion as the law requires me to do on all the relevant questions.

The bare facts of the case are that the assessee claimed that a loss of Rs. 24,528-1-9 in cotton business should be set off against his income from other sources. The Income-tax Officer recommended that this should be disallowed and the Assistant Commissioner disallowed it for reasons quoted above. He unnecessarily added "as my information is that assessee made great profit over it and not at all in loss". But when the case came in appeal before me, as para 2 of my appellate order will show, I refused to be influenced by the Income-tax

(1) 8 I. T. C. 255.

(3) 1 I. T. C. 266.

(2) 2 I. T. C. 514.

(4) 1 I. T. C. 416.

Officer's report or the Assistant Commissioner's remark mentioned above. I proceeded on the evidence that was brought on record. So far, therefore as the Appellate decision is concerned which is all that is germane to the present reference, I submit that such statements as that "the Income-tax Department proceeded on mere assumptions," or that "this method of assessing this income is based on mere assumption, hearsay information and suspicion", or that "the department believed that in 1924-25 the assessee was under-assessed", or that "he was asked to prove a negative" are based on a misapprehension.

8. According to the mercantile system of keeping accounts, which the assessee had been following, a computation of trading profits can only be made if the opening stock, the total purchases during the year, the total sales during the year, and the closing stock at the end of the year, are all known. The closing stock of one year forms the opening stock of the following year. Now for 1924-25 the assessee was assessed on an estimate, i.e., under section 23 (4) of the Income-tax Act, because his accounts for the year ending in Diwali 1923 had not been produced. When he produced his cotton accounts for the year ending in Diwali 1924, he claimed to have suffered a loss of Rs. 24,528-1-9 in that year. In these accounts only the total purchases during the year, the total sales during the year and the closing stocks were shown; but not the opening stock of the year (the closing stock of the previous year ending in Diwali 1923). The assessee had been doing cotton business under many names (khatas). In the account year, as seen from the Assistant Commissioner's assessment order, he did cotton business under seven khatas. In the preceding year, i.e., that ending in Diwali 1923, he had done business under the name of Dongulal Ghisulal also. Account books for the year ending in Diwali 1923 were called for by the Income-tax Officer in order to find out whether or not there was any balance of cotton at the close of that year which would form the opening stock for the year ending in Diwali 1924. On the 24th October, 1925, when assessee Radhakisan was questioned as regards these books, he stated "I shall show my 79-80 books to you on Monday to prove that no stock remained unsold at the end of Samvat 79-80." He did not produce these books before the Income-tax Officer, and the Income-tax Officer made the recommendations which have merited adverse comments. On the 17th December 1925 when questioned by the Assistant Commissioner on the same books, the assessee said evasively "The account books of the business done in the name of Dongulal Ghisulal are not found and I cannot produce them". When the assessee admitted that there were account books for the cotton business done in the previous year but actually did not produce them to enable the Income-tax Officer to find out whether any stock of cotton was left or not, the natural conclusion was that it was against his interest to do so and the legal presumption is obvious. This was the evidence on which the Department held that the loss in cotton claimed by the assessee was not proved. In coming to this conclusion the ordinary principle of evidence that the burden of proof is on the party which would fail if no evidence were produced which was enunciated in the case of *In re. Bishnu Priya Choudharani*(1), (which decision, I respectfully beg to state however, seems to me to be by no means above criticism), were not overlooked. On the other hand, they were strictly followed. It was not any negative statement of the assessee that the Department called on him to prove. It was his positive statement that he suffered a loss that he was called on and failed to prove. The facts of this case clearly distinguish it from the case of *Bishnu Priya Choudharani*. There estimated or assumed income was added by the Income-tax Officer. In the present case, a loss claimed by the assessee has been disallowed. The burden of proving this loss clearly lay, I submit, on the assessee. An assessee who claims a deduction must prove that he is entitled to it. He cannot, surely, simply assert that he has lost or spent so much, and by that bare assertion throw on the *Income-tax Officer*. (who I beg to suggest incidentally, is not a 'party' at all, but more like a judge, if

the analogy with real judicial proceedings is to be pressed) the burden of *proving a negative*. In the nature of the case it would practically always be impossible for the Income-tax Officer to discharge it. In the present case, the assessee, in a statement submitted along with the return under section 22 (2), stated that he suffered this loss in the cotton business, and to prove this it was necessary for him to show complete accounts for his cotton transactions including the opening stock for the year. His mere statement, though made on affirmation, that he had no opening stock was rightly rejected because though he has admitted the existence of account books for his cotton trade in the previous year, he did not produce them. This claim was correctly disallowed because the assessee failed to establish it.

9. In regard to the accounts produced and examined by the Department, it is observed in the High Court's order, that the Assistant Commissioner had found them correct and that the Commissioner of Income-tax seemed to have confused the assessee's cotton business with that done in the name of Dongulal Ghisulal in the previous year. I beg to point out that neither in the assessment order nor in the appellate order were the accounts produced criticised. What was stated in those orders was that the assessee, since he had not produced his previous year's account books, had failed to substantiate the alleged loss in cotton, which was therefore not allowed.

10. It seems to have been supposed that the Department did not allow the loss because it suspected that the assessee had suppressed the accounts showing his previous year's profits and the High Court has remarked that it is not likely that the Income-tax Department with its vigilant staff would have assessed this assessee's income from cotton business in the year 1923-24 at Rs. 26,000 only, when it was actually over Rs. 50,000 (Rs. 26,000 plus Rs. 24,528-1-9). I beg to submit that this was not the position of the Department. Had it been so, the Department would have had recourse to the simple expedient of revising under section 34 of the Income-tax Act the assessment made under section 23 (4) in the previous year. As already explained, the accounts of the previous year 79-80 ending in Diwali 1923 were called for in order to see whether they showed any closing stock.

11. I beg now to give my answers to the three questions raised in para 6 of the assessee's application dated February 1927:—*Question (a)*. My answer to this is that for the reasons given above I was correct in holding that the loss was not proved and that therefore it could not be admitted. *Question (b)*. For the reasons given above, this question should also be answered in the affirmative. *Question (c)*. No addition was made to the income but the loss claimed was disallowed and there was nothing unjustifiable or bad in law in this disallowance, nor was it based on suspicion or irregular or hearsay information.

W. B. Pendharkar, for the Assessee.

D. N. Choudhary, for the Crown.

JUDGMENT.

The Commissioner of Income-tax has stated this case according to the order of Kinkhede, Additional Judicial Commissioner, passed in Miscellaneous Judicial Case No. 8-B of 1927 on the 25th June 1928. The facts have been stated at some length in the reference and need only be briefly repeated. There is a firm at Akola styled "Raghunathdas Rampratap" of which the owner is Radhakisan Laxminarayan. That firm keeps accounts from Diwali to Diwali and submits

returns accordingly for the purpose of income-tax. For the year ending in Diwali 1924 the return shown was:—

	Rs.
Income	.. 10,473-12-6
Loss	.. 5,034-13-9
Total income	.. 5,438-14-9

The Income-tax Officer not accepting this return called for accounts and submitted a report to the Assistant Commissioner, who after hearing Radhakisan and examining the accounts, assessed the income at Rs. 44,847-6-0. Radhakisan made an appeal to the Commissioner of Income-tax and some reduction was made by the Commissioner, but otherwise the assessment was upheld. The assessee then applied for a reference under section 66 (2) of the Income-tax Act to the High Court, but his prayer was rejected by the Commissioner on the ground that no question of law arose out of the facts of the case. On an application then being made to this Court, Kinkhede, Additional Judicial Commissioner, held that the case involved questions of law and directed the Commissioner of Income-tax to state the case and make a reference.

The only point really in dispute now is whether the item of Rs. 24,528-1-9 shown as loss in the cotton business for the year under assessment is wrongly disallowed by the Assistant Commissioner making the assessment and by the Commissioner in the appeal. The matter has been stated at some length in the order of the Assistant Commissioner, dated the 17th December 1925, making the assessment, a copy of which is now on the record as Exhibit A. The point seems to be that in previous year cotton business was carried on in the name of Dongulal Ghisulal. When the books of the firm were called for, Radhakisan produced books of the firm of Raghunathdas Rampratap, but did not produce the books of Dongulal Ghisulal. He stated that he could not find those books and appears to maintain in his appeal and in his application to this Court that the accounts of Dongulal Ghisulal were incorporated in the books of the main firm Raghunathdas Rampratap. The Assistant Commissioner, however, held that he could not accept the loss of Rs. 24,528-1-9 because the closing stock and the sale proceeds of the preceding year were not shown. In the appeal the Commissioner also held, that as the accounts of the business in question, i.e., of Dongulal Ghisulal, were not produced, it could not be known whether there was any opening stock from the preceding year or not. The Commissioner therefore held that the appellant failed to prove that he sustained this loss, and did not allow it.

In his order of reference the Commissioner has pointed out that the ground given in the application to the High Court under section 66 (3) of the Act were distinct from the grounds given in the application to the Commissioner under section 66 (2), and contends that no reference upon a question of law not raised by the applicant before the Commissioner can be obtained, referring in this connection to the case decided by this court in the *Jainarayan Motiram v. Commissioner of Income-tax, Nagpur*(1), and to the case decided by the Madras High Court, *Thiruvengada Mudaliar v. The Commissioner of Income-tax, Madras*(2); and also to the decision of the Allahabad High Court *In the matter of Lalla Mal Hardeodas Cotton Spinning Mills*(3) and *In the matter of Makham Lal Ram Sarup*(4). The question whether an assessee can obtain an order of reference from the High Court upon a point of law not raised in his application to the Commissioner under section 66 (2) of the Act need not, we

(1) 3 I. T. C. 255.

(2) 2 I. T. C. 514.

(3) 1 I. T. C. 266

(4) 1 I. T. C. 416.

think, be gone into in disposing of the present reference, because, although the grounds given in the application to the High Court were different in form from the grounds given in the former application to the Commissioner, the real point at issue is the same viz., whether the Assistant Commissioner was right in disallowing the losses amounting to Rs. 24,528-1-9 alleged by the applicant during the year under assessment. The question of the interpretation of the Assistant Commissioner's order does not, in our opinion, arise, because the Assistant Commissioner's order is really clear and, in any case, the order of the Commissioner when deciding the appeal is as clear as possible and can leave no room for doubt that the losses were not allowed because they were held to be not proved, and not on account of any imaginary profits or gains which were supposed to have occurred during the year under assessment or the previous year.

The facts of the case are simple as stated above and in our opinion, the only point of law involved is the question on whom the burden of proof lies to prove losses alleged to have been sustained: on the party alleging the losses or on the Income-tax Department. The Assistant Commissioner and the Commissioner contend that the burden of proving losses is upon the assessee, who alleges them; whilst the argument put forward by the applicant is that proving losses is proving a negative, and that therefore, on the principle of the ruling in *Bishnu Priya Chowdhurani, In re* (1), the burden of proving the negative should not have been cast upon the applicant. This contention is, in our opinion, quite incorrect. There is a considerable difference between proving a negative, i.e., proving that there is no income during a year, and proving that there were, as a matter of fact, actual losses incurred. The applicant in the present case has not denied that there was income during the year under assessment. He has admitted income, but has pleaded that the expenditure exceeded the income and that a loss was sustained. He however, only stated the figures of purchases and sales, and when asked to give the opening balance, which was surely necessary so as to determine the net income for the year, he has failed to do so. We consider that, when once income has been admitted, the burden of proving losses is upon the assessee who alleges them, and the losses cannot be said to be satisfactorily proved unless all the particulars with regard to them are clearly shown and a very important particular with regard to such losses must always be the opening balance at the beginning of the financial year in which the losses are said to have occurred.

Under section 24 (1) of the Income-tax Act an assessee is entitled to have his losses set off against his income in any year, but he surely cannot claim that right unless he proves the losses; and the losses cannot, we think, be held to be satisfactorily proved by merely showing the figures for purchases and sales during the year without showing the opening balance in hand at the beginning of the year. Nor are we pressed by the argument that in the present case there is really an assessment for additional income during the preceding year, which view seems to have been taken by Kinkhede, Additional Judicial Commissioner, in his order directing the Commissioner to state the case. The income for the preceding year was assessed under section 23 (4) of the Act as the assessee did not produce his books or accounts. In the year now under review books were produced, but it has been held that those books, although they have been accepted as far as they go, are not sufficient to prove the losses alleged to have been sustained because the opening balance has not been shown. There is no attempt now made by the Income-tax Department to increase the assessment for the preceding year, nor has any action been taken under section 34 of the Act with regard to the previous year. All that is now held by the Income-tax Department is that during the year under assessment the applicant has really enjoyed income considerably

(1) I. T. C. 261.

more than the income shown, because the losses which he has alleged in his cotton business have not been proved.

The actual terms of the reference are:—(1) Was the Commissioner of Income-tax right in interpreting the Assistant Commissioner's order to mean that the loss was not proved notwithstanding the facts disclosed by the Assistant Commissioner's order dated 17-12-1925?

(2) Was the Commissioner of Income-tax right in interpreting the Assistant Commissioner's order to mean that no imaginary profits from a supposed stock were added in order to set off the loss of Rs. 24,528 sustained by the assessee?

(3) If not, was not the addition unjustified and bad in law as based on mere suspicion or irregular and hearsay information in the face of the assessee's statement denying the new and imaginary source of income?

With regard to the first, we are of opinion that the Commissioner of Income-tax was right in his interpretation of the Assistant Commissioner's order. In paragraph 2 of his order a copy of which is filed as Exhibit B, the Commissioner has quoted a passage from the order of the Assistant Commissioner and has then pointed out that there was some slight confusion in the latter order. The Commissioner has then gone on to show how the assessment in the preceding year was made under section 23 (4) as accounts were not shown, and in the year under assessment, as the opening stock had not been shown, the Assistant Commissioner refused to admit the loss of Rs. 24,528. The Commissioner has further explained that the addition of this loss to the income return is not really an assessment of additional income but is only a refusal to accept losses, which were alleged, but not proved. We cannot see that there is anything wrong or illegal in the Commissioner's interpretation of the Assistant Commissioner's order or in his findings.

As regards the second question, which is largely a repetition of the first, we would again hold that no imaginary profits from a supposed stock have been added either by the Assistant Commissioner's order or by the Commissioner's interpretation thereof. All that has been held in both orders is that, as the opening stock was not shown the losses which have been alleged as a result of the sales and purchases for the year under assessment could not be allowed. No imaginary profits or additional income have been assessed.

The figures as given by the assessee have been accepted with the exception that the losses shown have been disallowed as not proved.

From these findings it follows that the addition was not unjustified or bad in law. It was not really an addition of income, but only a refusal to allow alleged losses. Nor has it been shown that these losses have been disallowed on account of any hearsay information, and there is no question of any new or imaginary source of income. All that has been held is that in the ordinary cotton business, which was admittedly carried on by the assessee, the losses shown have not been proved, because the opening balance at the beginning of the year was not shown and only sales and purchases during the year were shown.

We are of opinion, then, that the case now stated for decision should be answered as indicated above and that there are no legal grounds for interfering with or reducing the assessment as made by the Commissioner of Income-tax. Costs of this application will be borne by the applicant. We fix pleader's fee at Rs. 300.

(286) IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Mr. Justice Lal Mohan Mukerji and Mr. Justice Niamat Ullah.

(15th February, 1929).

Messrs. Ram Kuar Mohan Lal

.. Assessee.*

v.

The Commissioner of Income-tax, United Provinces .. Referring Officer.

Income-tax Act (XI of 1922), Secs. 23 (4) & 27—Asst. on non-submission of return—Accounts filed in Criminal Court—Sufficiency of grounds for non-production—Refusal to re-open asst.

The assessee applied under Sec. 27 of the Income-tax Act for cancellation of an assessment made on the 28th January, 1928, under Sec. 23 (4) for non-submission of return, alleging the filing of his accounts in a pending criminal case as the reason for his default. The application was dismissed as the assessee did not show that he could not get the accounts by producing a copy of the application for the return of the accounts in the criminal case disposed of in October 1927.

HELD, that the Income-tax Officer was perfectly justified in refusing to re-open the assessment.

Case (Misc. Case No. 957 of 1928), stated under Sec. 66 (2) of the Indian Income-tax Act, by the Commissioner of Income-tax, United Provinces, for the opinion of the High Court.

CASE.

1. On June 11, 1927, the assessee—a joint Hindu family of Agra of which Lala Mohan Lal is the head—was served with notices under section 22 (2) of the Income-tax Act for making returns of his income on July 13, 1927, for the years 1926-27 and 1927-28.

On June 29, 1927, the assessee made an application dated June 28, 1927, for a month's extension which was granted. The grounds as urged in the application were that the proprietor of the firm had gone out on very urgent piece of business to Bombay, that the books of account were not ready, and that they would be brought up to date by the end of the extension applied for.

On July 15, 1927, he again made an application for an extension of two months. The grounds for extension urged in this application are practically the same as in the first, i.e., the proprietor's absence and the incompleteness of the books of account. The Income-tax Officer allowed only a month's extension, i.e., up to August 15, 1928.

The assessee did not make any return of his income on or before August 15, 1927, when the period of extension terminated, and the Income-tax Officer—without having issued a notice under section 22 (4), which it was not necessary to do—made a "best judgment assessment" under section 23 (4) on January 25, 1928 (i.e., 5 months and 10 days after the return had fallen due), on an income of Rs. 12,000 for the year 1926-27 (under section 34) and on Rs. 16,000 for the year 1927-28.

On January 27, 1928, the assessee made an application for the cancellation of the assessment on the ground, as stated in paragraph 2 of the application (please see copy of the application, Appendix A**), that the books of account

* (1929) 27 A. L. J. 536.

** Not printed.

had for a long time been detained in the court of the City Magistrate and that he could not get them back as the appeal, filed on behalf of the Government against the judgment of the City Magistrate, was still pending before the High Court.

The assessee was asked to adduce evidence in support of this application and the case was, therefore, postponed by the Income-tax Officer for this purpose. It was taken up on February 6, 1928, when Lala Shyam Sundar, a member of the assessee joint Hindu family, filed a printed copy of the judgment of the criminal case and his statement was recorded. It was alleged by him, in the course of his statement, that he had applied to the court for the return of the books but they had not been returned. The Income-tax Officer then gave him a further opportunity of producing evidence on March 12, 1928, to prove that he had actually made the application. The assessee appeared on this date and stated on oath to the effect that he had not been able to obtain copies of the application for the return of the books made before the City Magistrate and of the order passed thereon (please see extract copy of the translation of his statement contained in Appendix B.*). The Income-tax Officer then rejected the application for reasons given in his order dated March 13, 1928 (vide Appendix C.*). The assessee appealed against the order of the Income-tax Officer but the Assistant Commissioner of Income-tax agreeing with the Income-tax Officer dismissed the appeal (please see Appendix D.*).

2. The assessee has now demanded a reference to the High Court under section 63 (2) of the Income-tax Act for reasons given in the application (copy of the application is contained in Appendix E.*).

3. The question of law that the assessee wants the Commissioner to refer to the High Court are:—(1) Whether it is obligatory on an Income-tax Officer to issue a notice under section 22 (4) where a notice under section 22 (2) is served on assessee for the first time? and (2) Whether, in the circumstances of the case, the assessee “was prevented by sufficient cause” from making a return of his income within the meaning of section 27 of the Income-tax Act?

4. The first question does not arise out of the facts of the case as it was not raised in appeal and cannot, therefore, be referred.

5. As regards the second question, it is the opinion of the Commissioner that it is a question of fact and not of law: but, as divergent views have been held on this point by Coutts Trotter, C.J., and Krishnan, J., in *Shiva Pratap Bhattadu v. The Commissioner of Income-tax, Madras* (1), it is necessary that the question be referred for the decision of the High Court. The only question for reference to the High Court, therefore, is—Whether, in the circumstances of the case, the assessee “was prevented by sufficient cause” from making a return of his income within the meaning of section 27 of the Income-tax Act?

6. It is, I think, necessary to note here the salient features of the case.

It is a fact that Shyam Sundar, Mohan Lal and Nathi Mal, members of the assessee joint Hindu family, were involved in a criminal case during the year 1927-28 and the police enquiry and the subsequent trial in court under section 420 and 486, Indian Penal Code, extended over several months as would appear from the following extract from paragraph 1 of the judgment of the City Magistrate:—“On the report of the A. P. C. (Asiatic Petroleum Company) Inspector Wazir Mohammad Khan, dated June 24, 1926, and on a certificate from Mr. Blackwell of the A. P. C. firm, dated June 28, 1926, a case was registered and, after a protracted enquiry by the Police, a final report was submitted and sanctioned on March 17, 1927. On May 25, 1927, the accused through Babu Binde-

* Not printed.

(1) 2 I. T. C. 40.

shari Prasad, Vakil, served a notice on the A. P. C. claiming Rs. 40,000 as damages. This gave a fresh life to the affair and one of the A. P. C. officers visited the Superintendent of Police on June 28, 1927, and also sent a letter to him to re-open the matter and to make further enquiries. The matter was thus taken up again by the local Police and all the three accused were sent up under section 420, Indian Penal Code."

It is, however to be noted that the books of account were filed in the court of the City Magistrate, Agra, some time in July or August 1927, and the case was decided on October 15, 1927. (The exact date or month when the books were filed in the court of the City Magistrate is not known as in his statement of February 6, 1928, made before the Income-tax Officer the assessee mentioned this date to be July 1927, whereas in paragraph (b) of the statement of facts given in the application for reference, Appendix E, he has mentioned it as August). If the books were filed in August the assessee could easily prepare his returns of income before filing them (the books) in court.

Further, it has been alleged in the course of his statement made on February 6, 1928 (Appendix F.*), that the assessee had made an application for the return of the books about November, 1927. But he has failed to adduce any evidence in support of this fact before the Income-tax Officer. The allegation made in paragraph (c) of the statement of facts given in the application for reference (Appendix E) that the appellant did file a copy of the order of the Magistrate refusing to return the account books before the Income-tax Officer is incorrect as no such evidence was filed. This is also clear from the statement on oath made on March 12, 1928 by Shyam Sundar (Appendix B) in which he has admitted that he could not obtain a copy of the application made before the City Magistrate for the return of the books or of the order passed thereon. He has, no doubt, filed certified copies of an application of the same nature, and the order passed thereon, along with his appeal before the Assistant Commissioner of Income-tax, but these are the certified copies of an application made before the City Magistrate, Agra, for the return of the books on March 15, 1928, and of the order passed thereon and have nothing to do with the application alleged to have been made about November, 1927. There is, in fact, nothing on the record to show if any such application was ever made before the City Magistrate prior to the application of March 15, 1928. The application made on March 15, 1928, cannot affect the merits of the case as it was made long after the assessment had been disposed off. In fact, it was actually made after the application under section 27 had been rejected. Thus there is no evidence to show that he had made any application during the pendency of the assessment proceedings for the return of the books. It is further to be noted that the assessee could have referred to the books even as they were in the court of the City Magistrate, and that as the assessment was actually disposed off over three months after the criminal case had been decided he could easily have applied, soon after the decision of the case, either for the return of the books or for permission to refer to them in court for the purpose of making the return. The Commissioner is, therefore, of opinion that the answer to the question is in the negative.

JUDGMENT.

This is a reference by the learned Commissioner of Income-tax for an answer on the question, "Whether in the circumstances of the case, the assessee was prevented by sufficient cause from making a return of his income within the meaning of section 27 of the Income-tax Act?"

* Not printed.

The facts of the case are given in the statement of the case. The case is a very simple one. There was an assessment of income-tax to the best of the judgment, on 25th January 1928. The assessee applied for cancellation of the assessment under section 27 of the Income-tax Act. The assessment could be cancelled provided the assessee could prove that they were prevented by sufficient cause from making the return required by section 22 of the Income-tax Act. In this particular case it is said that there was a criminal case pending and the books of account had been produced in that case. The criminal case was disposed off in October 1927 and the best judgment assessment was made on 25th January 1928. The representative of the assessee's firm, who appeared before the Income-tax Officer, was asked to produce a copy of application that, he said, he had made for return of the books. He had over one month's time to do this, but could not produce a copy. In the circumstances, the Income-tax Officer refused to review his order. We think that he was perfectly justified.

Our answer to the question is in the negative.

We certify that the Government Advocate is entitled to a fee of Rs. 100. He may file his certificate within the month allowed under the rules.

(287) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Sir Murray Coutts Trotter, Kt., Chief Justice, Mr. Justice Odgers and Mr. Justice Beasley.

(15th February, 1929).

R. M. S. T. Ponnuswami Pillai

.. Assessee.

v.

The Commissioner of Income-tax, Madras

.. Referring Officer.

Income-tax Act (XI of 1922), Secs. 2 (1) & 4 (2)—Tea estate in Ceylon—Cultivation and manufacture on a large scale—Income from growing tea, if agricultural income—Remittance from Ceylon—Asst. as profits of business, legality of.

The assessee owned a tea estate in Ceylon, about 3700 acres in extent, employing more than 400 hands in pruning, weeding, plucking and other operations connected with the growing of the leaf. The green leaf when plucked was cured in his factory by up-to-date machinery manufacturing about 1 million lbs. of tea for sale in open market. On an assessment of a remittance to the assessee from Ceylon under Sec. 4 (2) of the Income-tax Act

HELD, that the income derived from the tea estate attributable purely to agricultural operations such as cultivating and plucking the tea leaf constituted the profits and gains of a business within the meaning of Sec. 4 (2) of the Act.

Case (O. P. No. 152 of 1928) stated under Sec. 66 (2) of the Indian Income-tax Act by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

CASE.

I have the honour to refer the following case for the opinion of the High Court under section 66 (2) of the Income-tax Act, XI of 1922.

2. The petitioner was a member of a Hindu undivided family represented by Mari Gounder, his grandfather. The joint family owned tea estates in Ceylon and a factory where the tea grown on the estates was manufactured for sale.

3. After the death of Mari Gounder, the petitioner and the other co-parceners of the family became divided in status but instead of dividing the estate and the other assets of the family between themselves by metes and bounds they continued to manage the properties jointly.

4. The total area covered by the tea estates in Ceylon—four in number—is approximately 3700 acres. They grow tea in these estates, employing more than 400 hands on pruning, weeding, plucking and other operations connected with the growing of the leaf. The green leaf when plucked is cured in their factory, in which up-to-date machinery is employed. In the factory they employ approximately 160 hands. The tea so manufactured amounts approximately to 1 million pounds. This is sold in the open market.

5. The total expenses of maintenance are deducted from the sale proceeds of the tea and the profit or loss arrived at on this basis is distributed among the petitioner and his co-sharers in proportion to the shares held by them in the joint family property.

6. The management of these estates is a commercial undertaking, carried on with a view to profit. The income is not a casual gain, or a result of the mere occupation of land.

7. During the year of account Akshaya, the petitioner received in British India a remittance of Rs. 58,000 from Ceylon. He did not deny that the remittance came out of the profits of the tea estates but contended that such income as it was first received in Ceylon could not again be received in British India and could not be charged to income-tax under section 4. The Income-tax Officer held that the petitioner with the other members of the family was carrying on the business of growers and manufacturers of tea, and that the profits received in British India were profits and gains of a business and should be deemed to accrue or arise in British India under sub-section 2 of section 4. On appeal the Assistant Commissioner agreed with the finding of the Income-tax Officer.

8. The question of law arising in the case, on which the opinion of the Court is solicited is "whether the income derived by the petitioner from his tea estates, in so far as it is attributable to purely agricultural operations such as cultivating and plucking the tea, constitutes profits and gains of a business." It may be assumed for the purposes of this reference, that the other conditions imposed by sub-section (2) of section 4 are satisfied and that the sum of Rs. 58,000 is liable to tax if the answer to this question is in the affirmative.

9. I am of opinion that the growing and manufacturing of tea in the manner described above constitutes a business within the meaning of the definition contained in section 2, sub-section (4) of the Indian Income-tax Act, 1922, and that the whole of the income derived therefrom is "profits and gains of a business."

The petitioner's contention is that the profit derived from his tea estates is in part attributable to the growing of the leaf, which is an agricultural process, and that this agricultural process cannot be a business or part of a business. In my opinion the agricultural process is, on the facts of this case, an inseparable part of the business upon which the petitioner is engaged, and should not be treated as a distinct source of income.

It is common ground that the income attributable to the coconversion of the green leaf into a marketable product is business profit, being derived from a process of manufacture. If the petitioner's contention is accepted it will be necessary to determine what amount or proportion of his income is attributable to this process, and whether the sum so attributable, or any part of it, has been received in or brought into British India.

The petitioner relies upon the ruling in the case of the *Killing Valley Tea Company v. Secretary of State for India*(1), in which it was decided that the income derived by the said Company from tea estates was in part attributable to agriculture and to that extent was "agricultural income" according to the definition contained in section 2 (1) of the Income-tax Act. The question whether agriculture was or could be part of a business did not arise in that case because "agricultural income", as defined in the Act, would be exempt from tax even if it were found to have been derived from a business. We are admittedly not now concerned with agricultural income in this sense at all.

A. Krishnaswamy Iyer, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

The question referred to the Full Bench is whether the income derived by the petitioner from his tea estates, in so far as it is attributable to purely agricultural operations such as cultivating and plucking the tea, constitutes "profits and gains of a business".

The petitioner and the other co-parceners of his family, though divided in status, have not divided by metes and bounds certain tea estates in Ceylon, but have continued to manage them jointly. Those estates are four in number and the total area of them is approximately 3700 acres. More than 400 hands are employed in pruning, weeding, plucking and other operations connected with the growing of the leaf. The green leaf when plucked is cured in a factory by up-to-date machinery. In the factory there are employed 160 hands and the tea so manufactured amounts approximately to one million lbs. and is sold in the open market. During the year of account the petitioner received in British India a remittance of Rs. 58,000 from Ceylon. It is admitted that this sum was remitted out of the profits of the tea estates. The Income-tax Officer has assessed the petitioner to income-tax under section 4 (2) of the Indian Income-tax Act, which is as follows: Profits and gains of a business accruing or arising without British India to a person resident in British India shall if they are received in or brought into British India, be deemed to have accrued or arisen in British India and to be profits and gains of the year in which they are so received or brought, notwithstanding the fact that they did not so accrue or arise in that year, provided that they are so received or brought in within three years of the end of the year in which they accrued or arose. On appeal the Assistant Commissioner agreed with the findings of the Income-tax Officer. The assessee however contends that the profit derived from the tea estates is in part attributable to the growing of the leaf which is an agricultural process and that this agricultural process cannot be described as a business and therefore the profit upon which the income-tax is sought to be imposed is not the "profit or gain of a business" and so cannot be taxed.

The question we have to decide is whether growing tea is a business in the sense that that word is used in section 4 (2) of the Indian Income-tax Act. The definition section of the Act is section 2 and in sub-section (4) "business"

is defined as including "any trade, commerce or manufacture or any adventure or concern in the nature of trade, commerce, or manufacture." In sub-section 1 of the same section "agricultural income" is defined. The assessee contends that the process of growing tea, as distinct from the process of converting green leaf into tea, is agriculture as defined by section 2 (1) (b) and that the income is agricultural income which, had it been derived from tea estates in British India, would have been exempt from taxation under section 4 (3) (viii). He does not of course in respect of this income claim exemption under that section. He cannot do so as the tea estates are in Ceylon; but his contention is that in India such an income is agricultural income, that the process which produces it is agriculture and that the description of "business" in section 2 (4) was never intended to be applied to this exempted process wherever the income from it is derived, but that it is income either from "property" or "other sources."

Mr. Aladi Krishnaswami Ayyar relies on the case of *Killing Valley Tea Company v. Secretary of State for India*(1). There the question considered was whether the income from a tea garden, where tea was grown and made ready for the market by mechanical process, was assessable, and it was held that the income was to be apportioned and so much of it as was obtained by the manufacturing process was assessable and so much of it as was obtained by the process of growing was exempt as being agricultural income. In apportioning the income the Calcutta Bench adopted the principle in the case of the *Inland Revenue Commissioners v. Ransom*(2), and other cases. In the former case the respondents, who were a limited company carrying on business as manufacturing chemists and growers of medicinal and other herbs, owned a factory where the manufacture and distillation of herbs were carried on, and they also occupied a farm on which they grew herbs for treatment in the factory. Memoranda were kept of the value of the produce transferred to the factory, of the prices obtained by the sale of incidental crops to the public, and of the expenses relating to the farm operations. The respondents were assessed to excess profits duty, and on an appeal by them against the assessment the General Income-tax Commissioners found as a fact that the respondents occupied the farm mainly for the purpose of the factory, but they were of opinion that the occupation of the farm was the business of husbandry, and that the profits of the farm should be excluded for the purpose of excess profits duty, and they fixed the assessment on this basis. It was held that on the facts there was evidence on which the General Commissioners could find that the company was engaged in husbandry and also that it was possible for the Commissioners to separate the business of husbandry from other businesses, there being nothing in law to prevent them from doing so. It is quite clear that where more than one process is used, each can be kept distinct from the other or others for purpose of assessability to income-tax. One process may be exempt from taxation altogether, another may be assessable under one section of the Act and another under another section and that apportionment was made in *Killing Valley Tea Company's case*(1). With regard to the assessment of tea estate in India it is the practice to so apportion the income from those estates, that is to say, a portion of the income is treated as agricultural income and exempted from taxation and the remainder is assessed to tax. Important though the decision in *Killing Valley Tea Company's case*(1), may be as deciding that the profit from the mere growing and tending of the tea is agricultural income, it has no real bearing upon the question which is before us. That case did not decide that agriculture is not a business; it merely decided that income derived from growing tea is "agricultural income". It follows that such income is exempt from taxation on that account because section 4 (3) (viii) expressly exempts it. The Calcutta Bench do not consider whether the income was income falling within any other section of the Indian Income-tax Act and

(1) 1 I. T. C. 54.

(2) (1918) 3 K. B. 708.

leave quite undecided the question of whether this process can be described as a business or not.

Mr. Alladi Krishnaswami Ayyar relied also upon *Back v. Daniels*(1). There the respondents, who were wholesale potato merchants and potato salesmen carrying on business in London, owned land on which they grew potatoes, and also hired land under ordinary tenancy agreements for the same purpose. They also grew potatoes on land in Lincolnshire which they hired from neighbouring farmers under special agreements, the lands so hired being changed each season. Under those special agreements by which the land was purported to be let to the respondents, the respondents had possession of the land until the potatoes were fully ripe, which in some cases was more than a year from the date of the agreement and in others was less than a year. The landlord under the agreement had to plough the land, do all the carting and provide all the horse labour that was necessary. The respondents supplied all the seed, artificial manure, and manual labour necessary to grow the manure, plant the seed, take up and pit the potatoes and afterwards prepare them for the market. The landlord was paid £3 per acre as rent for the land and £15 per acre for supplying all horse labour, etc., which sum also included all rates and taxes. The landlord was, and the respondents were not, assessed to income-tax under Schedule B in respect of those lands. The respondents sold the potatoes which they had grown in the course of their business as potato salesmen. They were assessed in London to income-tax under Schedule D on the profits of their business as potato merchants and salesmen, and the profits they made from the sale of potatoes grown on the lands under those special agreements were included in that assessment. It was held that the respondents had the use of the lands on which they grew potatoes under the special agreements in a full sense of the term, with full power to maintain their rights and must therefore be deemed to be occupiers within rule 2 of Schedule A and that they were assessable in respect of the profits arising from the occupation of the lands in question under Schedule B and not under Schedule D.

Under the English Income-tax Act of 1918 the tax in respect of the occupation of all lands, tenements, hereditaments and heritages in the United Kingdom for every 20sh. of the assessable value thereof is chargeable under Schedule B of that Act and by rule 5 of the Schedule any person occupying lands for the purpose of husbandry may elect to be assessed under Schedule D and in accordance with the provisions and rules applicable thereto instead of under Schedule B. The respondents in that case (the assessee) contended that they were for the purpose of the Income-tax Acts to be deemed occupiers of the lands so used by them. They had not exercised their option to be taxed under Schedule D and claimed that the potatoes were grown by them and produced as the result of their occupation of the lands and that while they were liable to be assessed under Schedule B in respect of this occupation the potatoes so grown could not be distinguished from any other produce of husbandry marketed in the ordinary course and that the profits from the sale of them could not be included in any assessment under Schedule D. With those contentions the Court of Appeal agreed. It may be observed however that the occupation of husbandry is specially dealt with in the English Income-tax Act and even in such occupations it is open to the person so engaged at his option to be assessed under Schedule D as carrying on a business. There is no such special treatment in this country of the occupation of agriculture except that the income arising therefrom is exempt altogether from taxation. There is no equivalent here of Schedule B of the English Income-tax Act of 1918 and it is also of importance to observe that cultivating land to grow produce for the purpose of sale is considered in *Back v. Daniels*(1) by Scrutton, L.J., to be a trade. On page 203 he states as

(1) 9 Tax Cas. 183; (1925) 1 K. B. 526.

follows: "Cultivating land to grow produce for the purpose of sale is in my opinion a trade. But Parliament had dealt with that trade where it is exercised by the occupation of land, by assessing the occupier on the annual value of the land and not on the profits made out of its produce, unless the occupier himself elects to be so taxed. When there is a separate and distinct operation unconnected with the occupation of the land, such as cheese factory dealing with the milk of a dairy farm, or a butcher's shop dealing with the beasts of a cattle farm, I can understand a separate assessment of that operation; but I do not think that the fact that the farmer sells his produce either on the farm or at the local market, or at Mark Lane, or even if he sells it in a shop, justifies an assessment under Schedule D as well as or in substitution for Schedule B."

As Scrutton, L.J., points out although cultivating land is a trade Parliament has especially dealt with that trade, namely, by allowing the person who carries it on to be assessed at his option either under Schedule B as occupier of land or under Schedule D as a person carrying on business and in addition to persons engaged in husbandry being given the option of assessment under either Schedule B or D, persons occupying woodlands are also under the rules of Schedule B of the English Income-tax Act of 1918 given a similar option. Under rule 7 any person occupying woodlands who proved to the satisfaction of the General Commissioners or the Special Commissioners that those woodlands are managed by him on a commercial basis and with a view to the realisation of profits may elect to be assessed and charged the tax in respect of those woodlands under Schedule E instead of under Schedule B as a person occupying lands for the purpose of husbandry only.

Mr. Alladi Krishnaswami Ayyar's argument is that this income arises from "property", namely, section 9 (1) of the Indian Income-tax Act and he uses the case of *Back v. Daniels*(1), as an argument in support of this contention. But it seems to me that there is the distinction that the English Income-tax Act of 1918 expressly provided for the occupation of husbandry being included in Schedule B and dealt with as profits from the occupation of land; and even under that Act husbandry can be treated as a business at the option of the person who is engaged in it. Husbandry has been described as a business in a case already referred to, namely, *Inland Revenue Commissioners v. William Ranson & Co.*(2), where Sankey, J., described it as a business. On page 713 he says "The second question is whether the General Commissioners had any authority to separate the business of husbandry from the other business carried on by the respondents. This question is one of some difficulty. It is said for the Crown that there is no authority for separating the subsidiary business of husbandry from the main business of manufacturing drugs and for saying that the respondents are not liable to excess profits duty in respect of the business of husbandry while they are liable to the duty in respect of their main business."

Another case relied upon by Mr. Alladi Krishnaswami Ayyar was *Commissioner of Inland Revenue v. Sangster*(3). In that case the respondent had for many years been an inventor and had been granted nearly 400 patents. Of these he had only sold one, and that was about 25 years ago. He was managing director of a company which worked certain of his patents and paid him a fixed salary and commission dependent on results, and he was also managing director of, and preponderant shareholder in, another company of which he was the promoter and which paid him royalties on non-exclusive licenses in respect of certain of his patents granted by him to the company. He was also a director

(1) 9 Tax Cas. 183; (1925) 1 K. B. 526.

(3) (1920) 1 K. B. 587.

(2) (1918) 2 K. B. 709.

of several other manufacturing companies and, it was held by Rowlatt, J., that he was not carrying on a trade or business within the meaning of section 38 (1) of the Finance (No. 2) Act of 1915, so as to be liable to the excess profits duty imposed by that section. On page 597, Rowlatt, J., says, "Now the respondent does not sell his patents. He sold one 25 years ago, but it is quite clear that that is not the way in which he deals with the product of his inventive ability. He simply keeps on inventing things and keeping the patent in his own hands, making what he can out of it by granting licenses, just as a man builds a house and makes something out of it by letting it. Of course a painter cannot, as things are, do otherwise than sell his pictures. An author is more like an inventor, because he can grant licenses under royalties. It seems to me that the true position is that, unless it can be shown that the property called into existence by the invention, or by the painting, is sold so as to obtain a money return against it, no evidence is produced that the inventor or the artist is carrying on a business. If the artist or the inventor sells the product of his ability, in many cases enquiry would have to be made whether he does so habitually so as to bring him within the category of persons who carry on a business, but if he does not sell at all I do not think there is any evidence in support of the contention that he carries on a business." And further on he says: "It seems to me that carrying on a business involves, in a case like this, the disposal of the article which is produced as opposed to retaining it as a valuable thing in itself which can be treated as an investment, just as anything bought with the money obtained for it if it had been sold could be treated as an investment." I do not think that this case is at all helpful to Mr. Alladi Krishnaswami Ayyar.

Mr. Pantanjali Sastri argues that agriculture is a business as defined by section 2 (4) of the Indian Income-tax Act. He describes it either as a trade or a business or an adventure or concern in the nature of a trade. One of the cases upon which he relies is *Vallambrosa Rubber Co., Ltd., v. Farmer* (1), a decision of the Court of Session (Scotland). That was the case of a rubber company with plantations owned and worked by it in the Federated Malay States and the question which arose in that case was what deductions the company was entitled to make in respect of expenditure for superintending, weeding, etc., of the plantations. Rubber trees do not yield rubber until they are about six years old. Consequently the company earned no profit at all during those years but nevertheless the rubber trees had to be cultivated during that time and expenditure incurred for doing so, much in the same way as tea trees have to be cultivated and looked after before they produce the green leaf which is converted into tea. The question which arose in that case was whether the company was entitled to deduct the whole of its expenditure for superintendence and weeding on the estate for each year or whether the deduction was to be limited to one-seventh of the expenditure only, that is to say, as there were no profits during the six years in which the rubber trees were attaining maturity it was argued by the Crown that although expenditure had been incurred for each year the deduction was to be proportionate only on the number of years which the trees took to become profit earning. It was held however that the company was entitled to deduct all the expenditure for each year notwithstanding the fact that no profits were earned during those years and the deductions the company was held entitled to make were deductions allowable under Schedule D of the English Income-tax Act.

It will be seen therefore that although the business carried on by the company might have been divided into two parts, namely, that of cultivating the trees and that of turning the produce of the trees into rubber the whole process was treated as a business and no attempt was made to argue that the process of culti-

(1) 5 Tax Cas. 529.

vation was assessable in any other way than as a trade. I cannot myself see any distinction between cultivating trees upon which the tea leaf is grown for the purpose of that leaf being converted into tea and sold and the process of cultivating trees for the purpose of converting the juice from those trees into saleable rubber. Both seem to me to be a business. Cultivating the tea tree is of no value to the cultivator unless the green leaf is turned into tea in the factory and the factory is of no value unless the green leaf is produced by cultivation. The two are, in my view, parts of one whole and it seems difficult to say that one part is a business and the other not. The cultivation of the tea tree is an integral part of the whole business. If a company were to be formed for the purpose of making tea and selling it at a profit, that would be the trade, manufacture, adventure or concern of the company and the whole operation whether it be cultivation or production of the tea would be so. Lord Johnstone in the *Vallambrosa case*(1) says: "The rule primarily to be applied is the first Rule for both the first and second cases under the schedule, which says, in estimating the balance of profits or gains, that is the net profits to be charged, no allowance should be made except for money wholly or exclusively laid out or expended for the purpose of such *trade, manufacture, adventure or concern*. This must be ascertained from the Memorandum of the company, read in conjunction with the actual operations of the company. Some of the purposes of the memorandum are obtained by capital, some by revenue expenditure. In making the discrimination, certain items will no doubt be found to come very near the dividing line, but the discrimination must nevertheless be made as best may on business lines. It appears to me that, as at present worked, the *trade, manufacture, adventure or concern* of the company is the cultivation and production for sale at profit of rubber and other tropical products. For this purpose land had to be acquired, cleared, and drained, roads made, and buildings erected, before the cultivation began. What was expended for these purposes was, I think, capital expenditure, and not, in the sense of the Income-tax Act, money laid out and expended for the purposes of the trade. But once the cultivation began with the planting, expenditure on cultivation production, and marketing was I think revenue expenditure for the purposes of the trade."

I cannot think that, had the Vallambrosa Rubber Company Limited been a tea company instead of a rubber company, the decision would have been otherwise. In order to decide definitely the Court of Session must have held that whereas weeding rubber plantations and tending the trees is a trade, weeding tea plantations and tending the bushes is not a trade. For the reasons I have stated I would answer the question referred to us in the affirmative. Rs. 250 costs to the Commissioner of Income-tax.

(288) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Sir Murray Coutts Trotter, Kt., Chief Justice, Mr. Justice Odgers
and Mr. Justice Beasley.

(18th February, 1929).

English and Scottish Joint Co-operative Wholesale Society, Ltd. Assesseees.

v.

The Commissioner of Income-tax, Madras.

Referring Officer.

Income-tax Act (XI of 1922)—Mutual Co-operative Society—English and Scottish Co-operative Wholesale Society Ltd.—Shares held by constituent co-operative societies—Society owning estates and selling produce to members—Profits

(1) 5 Tax Cas. 529 at p. 586.

distributable proportionate to purchases—Payment of interest on share capital—Society, if earning profits assessable to tax.

The English and Scottish Co-operative Wholesale Society Ltd., incorporated in England under the Industrial and Provident Societies Act, 1893, had all its shares owned exclusively by two other co-operative societies. The object of the Society inter alia was to carry on the business of planters, growers, producers, merchants and manufacturers, commission agents and brokers of tea..... and any other trade or business which might seem calculated to conduce to the more efficient.....working of the said business. Under the rules of the Society, any profit shown in the balance sheet was to be applied inter alia in paying interest on share capital at a rate not exceeding 6 per cent. and in paying dividend in proportion to the amount of purchases made by members from the Society.

The Society owned large estates in India growing tea, pepper and other produce, the produce so raised, except as to a small part sold locally as unfit for export, being sold to the members at the prevailing market rates, though the rules did not prohibit sales to non-members.

On an assessment to income-tax, the Society contended that it was not carrying on any business in British India, that it was not chargeable on that portion of the profits made through dealings with its members and that in any case the surplus derived by it from transactions with its own members was not chargeable under the Income-tax Act.

HELD, that the Society was a purely mutual co-operative society making no profits, coming with the ruling in New York Life Assurance Co. v. Styles and hence not liable to be assessed to income-tax.

Case [O. P. No. 134 of 1928; Referred Case No. 6 of 1928] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

CASE.

I have the honour to state the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (2) of the Indian Income-tax Act, 1922.

2. The applicant, The English and Scottish Joint Co-operative Wholesale Society Ltd., is a Society incorporated in the United Kingdom under the Industrial and Provident Societies Acts with an unlimited capital divided into shares of the value of £5 each. A copy of the Rules of the Society, marked Exhibit "A"* is annexed hereto and forms part of the case.

3. The objects of the Society as set out in Rule (2) are *inter alia*:—"To carry on the business of planters, growers, producers, merchants and manufacturers, commission agents, and brokers of tea, coffee, cocoa and foreign and colonial produce in all their branches, and any other trade or business which may seem calculated to conduce to the more efficient and/or profitable working of the said business".

4. Rule 5 provides that the Society shall consist of the Co-operative Wholesale Society, Ltd., and the Scottish Co-operative Wholesale Society Ltd., but rules 7 and 8 contemplate the admission of other members also. The shares of the Society may be transferred or withdrawn under certain conditions (Rules 6 & 7). The Committee of management may from time to time obtain loans and

receive money on deposit from members of the Society or otherwise, issue bonds under the seal of the Society or grant other documents of debt bearing interest (Rule 18). The capital and funds of the Society may be invested in the purchase or on the mortgage of lands, buildings, shares and securities (Rule 19).

5. Rule 20 provides that in the event of the balance sheet showing a profit in favour of the Society after paying or providing for all the expenses of management and the interest on loans the profits shall be applied as follows:— (a) In the depreciation of the original value of land (except agricultural land and tea gardens) at not less than $\text{£}1\frac{1}{4}$ per cent. per annum, buildings at not less than $\text{£}2\frac{1}{2}$ per cent. per annum, of fixed stock at not less than $\text{£}5$ per cent. per annum, and of live or rolling stock at not less than $\text{£}15$ per cent per annum. (b) In paying interest on the share capital at such rate not exceeding $\text{£}6$ per cent. per annum as the half-yearly general meeting may from time to time determine. (c) In appropriating a sum of not less than $\text{£}5$ per cent. of the net profits to a reserve fund, which shall be applied for the benefit of the society in manner determined by a general meeting of the society. (d) In appropriating a sum not exceeding $\text{£}1\frac{1}{4}$ per cent. of the net profits to a special fund for the purpose of making grants to any purpose whatsoever (other than the purposes herein-before specially mentioned) which the general meetings may from time to time determine whether such purpose be within the objects for which the society is formed or not. (e) In payment of a dividend to the members rateable in proportion to the amount of purchases made by them from the society. (f) The remainder, if any, shall be carried forward to the next account.

6. By Rule 22 (a) the Society may by a resolution of a general meeting acquire and undertake the whole or any part of the business goodwill and assets of any person, firm, company, or society carrying on or proposing to carry on any of the businesses which this Society is authorised to carry on and as part of the consideration for such acquisition may undertake all or any of the liabilities of such persons, firm, company or society.

7. The Society owns large estates in India on which are grown tea, pepper, cardamom and other products. The produce so raised, except a small part which is not fit for export and which is sold locally, is sold to its members who at present are the Co-operative Wholesale Society Ltd., of England and the Scottish Co-operative Wholesale Society Ltd., of Scotland, at the prevailing market prices. The rules do not prohibit the sale of produce to persons other than members of the Society; but the local manager of the Society has stated on oath that sales are confined to its two members.

8. The Society maintains accounts in India showing the expenditure incurred in its various departments and the receipts from the sale of its products. The only income of the Society chargeable to income-tax is that derived from the manufacture and sale of tea. This income is determined in accordance with the provisions of Rule 24 of the Rules framed by the Central Board of Revenue in exercise of the powers conferred on it by section 59 of the Indian Income-tax Act, 1922.

9. For the assessment of the year 1926-27 the Society made a return of its income to the Income-tax Officer, Ootacamund but contended that it was not carrying on any business in British India, that it was not chargeable to income-tax on that portion of the profits which it made through dealings with its members or shareholders and that in any case the surplus derived by it from transactions with its own members is not profits and gains chargeable to income-tax within the meaning of the Income-tax Act. The Income-tax Officer held that the Society was carrying on business and levied tax on an income of Rs. 1,56,649.

10. The Society appealed to the Assistant Commissioner who upheld the Income-tax Officer's view. A copy of the Assistant Commissioner's order is appended—Exhibit B.*

11. The Society has required me under section 66 (2) of the Income-tax Act to refer the following question for the decision of the High Court. "Whether the profits derived by the English and Scottish Joint Wholesale Co-operative Society constitute income liable to tax under the Indian Income-tax Act."

12. In computing the profits of the Society the Income-tax Officer excluded a sum of £23,857-13-6 or Rs. 3,23,942 paid as interest on the capital of the Society employed in British India. As I considered that the Income-tax Officer was wrong in allowing this interest, I called upon the Society to show cause why I should not revise the assessment under section 33 of the Income-tax Act. It is contended on behalf of the Society that the liability to pay such interest is a contractual liability imposed by Rule 20 of the Society's rules and constitutes a continuous demand in respect of its business, that the payment is necessary to enable the Society to carry on its activities and that it is an expenditure solely incurred for the purpose of earning its profits and gains within the meaning of section 10 (2) (ix). At the request of the Society I refer the following further question for the decision of the High Court under section 66 (1) of the Income-tax Act.

"Is the sum of Rs. 3,23,942 paid by the Society to its shareholders under Rule 20 (b) of its rules an expenditure necessary to earn its profits within the meaning of section 10 (2) (ix) of the Income-tax Act.

13. *First question.* I am of opinion that the Society is an ordinary trading concern and that it is liable to be assessed on the profits and gains derived by it in the course of its business. The Society has not been constituted to have dealings with its own members and in fact there is nothing in the rules of the Society precluding it from having dealings with persons other than its members. The Society has a capital divided into shares. The net profits of the Society are used (1) in paying interest on capital which is in the nature of a dividend on shares and (2) in paying a second dividend to members purchasing the produce of the Society proportionate to their purchases. It may happen that a member who has subscribed capital may not purchase anything from the Society, in which case the share of profits paid to him by way of interest on capital cannot be said to be a return of the surplus of any money paid by him to the Society in the course of his dealings with the Society. The Society claims on the strength of the ruling in *Styles v. New York Life Assurance Company*(1), that the "surplus from trading" is not income liable to tax. I am of opinion that the case is on all fours with the later case of the *Liverpool Corn Trade Association v. Monks*(2), followed by the Madras High Court in the case of the *Trichinopoly Tennore Hindu Permanent Fund*(3) and that the profits of the Society arising in British India are liable to income-tax under the Indian Income-tax Act.

14. *Second question.* It is admitted that the sum on which the alleged interest has been paid is the capital of the Society contributed by its shareholders. Rule 20 states "In the event of the balance sheet showing a profit in favour of the Society after paying or providing for all the expenses of management and the interest on loans, the profit shall be applied as follows: * * * * (b) In paying interest on the share capital at such rate not exceeding £6 per cent. per annum as the half yearly general meeting may from time to time deter-

* Not printed.

(1) 2 Tax Cas. 460, 14 App. Cas. 381.

(2) 10 Tax Cas 442 ; (1926) 2 K. B. 110.

(3) 2 I. T. C. 386.

mine." I am of opinion that the sum of Rs. 3,23,942 distributed as "interest" among the shareholders is part of the profits and gains which the Society had earned by the use of its capital and that such profits are liable to be taxed in the hands of the Society irrespective of the mode of their subsequent application. The fact that the Society makes over a part of its profits to its shareholders in the shape of interest on the capital contributed by them does not make the payment an expenditure necessary to earn the profits within the meaning of section 10 (2) (ix) of the Income-tax Act.

Nugent Grant, for the Assessee.

M. Pantanjali Sastri, for the Crown.

JUDGMENT.

ODGERS, J.:—This is a case stated for our opinion by the Commissioner of Income-tax, Madras, and the question is whether the Society is carrying on a business from which it derives profits or gains, or whether, on the other hand, it is a mutual co-operative society earning no profits and therefore not liable to assessment under section 60 of the Act and the notification of the Government of India published on 25-8-1925 which runs as follows:—"R. Dis. No. 291 I.T./25.—In exercise of the powers conferred by section 60 of the Indian Income-tax Act, 1922 (XI of 1922), and in supersession of the Notifications of the Government of India in the Finance Department No. 681/F., dated the 28th December 1922 and No. 718-F., dated the 8th March 1922, the Governor-General in Council is pleased to direct that the following class of income shall be exempt from the tax payable under the said Act, namely:—"The profits of any Co-operative society other than the Sanikatta Salt-owners' Society in the Bombay Presidency for the time being registered under the Co-operative Societies' Act, 1912 (II of 1912), or the dividends or other payments received by the members of any such society on account of profits."

The Society was incorporated in England on the 31st December, 1923 under the Industrial and Provident Societies Acts of 1893 and the shares are owned exclusively by two other Co-operative Societies, viz., the Co-operative Wholesale Society of England and the Scottish Co-operative Wholesale Society of Scotland. The capital is £2,400,000. For the year 1923-24, the Collector of the Nilgiris assessed this Society to tax. On the 29th September 1923, Mr. Strathie, the then Commissioner, held that the greater part of the profits were derived from a mutual fund and cancelled the assessment. In the years 1924-25 and 1925-26 there was no assessment but in the year 1926-27 the Income-tax authorities raised the question as to the year 1925-26.

It is admitted for the Crown, that, had the Society been registered in India, it would undoubtedly be exempt under the notification made by the Governor-General under section 60 of the Act of 1922 set out above.

The Society maintains that it is a mutual society making no profit but returning to its members merely the difference between the amount notionally debited to them and the saving that the Society has been able to effect by its operations and that difference is distributed by way of bonus to the members of the Society.

The Commissioner was of opinion that the Society was an ordinary trading concern and that there is nothing in its rules to preclude it from having dealings with persons other than its members. The reasons that induced the Commissioner to come to this decision appear to be that the profits of the Society are utilized in paying interest on capital which is in the opinion of the

Commissioner a dividend on shares and, secondly in paying another (second) dividend to members purchasing the produce of the Society in proportion to their purchases. The Commissioner adds that supposing a member, who has subscribed capital, makes no purchases, the share of produce paid to him by way of interest cannot be said to be a return of the surplus of any money paid by him to the society. The Commissioner further notes that the society relies on *Styles' case*(1) but he was of opinion that this case is governed by the *Liverpool Corn Trade Association, Ltd. v. Monks*(2). The question therefore turns really on the nature of the Society's constitution. I shall not set out the rules in any detail but refer to them by number with just a word of explanation of their contents.

Rule 5 as to members, states that the Society shall consist of the Co-operative Wholesale Society Limited and the Scottish Co-operative Wholesale Society Limited.

Rule 6. The shares of the Society shall be £5 each and unlimited in number.

Rule 7. Application for shares must be made after resolution passed at a meeting of the Society making the application.

Rule 14. The committee of management is to consist of eight persons, 6 appointed by the Co-operative Wholesale Society Limited and 2 by the Scottish Co-operative Wholesale Society Limited. These persons must be members of the general committee of management of the society appointing them.

Rule 18. The committee of management has power to borrow provided the loans do not exceed 10 times the amount of the subscribed capital of the Society for the time being and the interest not to exceed 5 per cent.

Rule 20. Division of profit. This perhaps is the most important rule. If the balance sheet shows a profit it is to be applied as follows:—(a) In the depreciation of the original value of the land; (b) In paying interest on the share capital at a rate not exceeding 6 per cent; (c) In appropriating a sum of not less than 5 per cent. to a reserve fund; (d) In appropriating a sum not exceeding $1\frac{1}{4}$ per cent for the purpose of making grants; (e) In payment of a dividend to the members rateably in proportion to the amount of purchases made by them from the Society.

It is (b) and (e) of these sub-rules that are particularly relied on by the Crown and especially (b) which is said to indicate with certainty the carrying on of an ordinary business with share capital on which dividends are paid. On the other hand, the Society contends that these payments of interest on the share capital are simply a return of part of the profit to the members and as for the objection that the Society might consist of more members than the two prescribed in Rule 5 it is to be observed that any member of the Society must be a co-operative society itself. There is no evidence before us that any other members have been admitted to membership except the two societies named in Rule 5 in relation to which the Society in question is termed the 'apex' society and it appears to me that in a case of this sort we are not concerned with possibilities and that it must be taken that the two societies were in the year of account the only members. The test of a mutual society laid down, in section 39 (4) of the Income-tax Act of 1918 are (1) selling to its own members (2) the number of shares must be unlimited.

(1) 2 Tax Cas. 460, 14 App. Cas. 381.

(2) 10 Tax Cas. 412; (1926) 2 K. B. 110.

A certain amount of tea, etc., produced by the Society is sold in India if it is found not worth the expense of exporting. It is admitted that the Society is liable to be assessed on these local sales in India. Otherwise, the produce of the Society is sent in its entirety to the United Kingdom and is disposed of there by the two constituent societies.

I shall now consider the cases which have been cited in some detail in order that the points supporting the one side or the other may be clearly brought out. The two cases on either side of the line which govern the question are *Styles v. New York Life Assurance Co.*(1), and *Last v. London Assurance Corporation*(2). Accordingly, the question here is under which of these cases and the principles enumerated thereunder does the present case fall?

I shall first examine *Styles v. New York Life Insurance Company*(1). That insurance company had no share or shareholders and the members were the holders of participating policies. The amount claimed by the Company from each of the policy-holders was an amount calculated as necessary to cover expenses and payment of policies, etc., and if it was found at the end of a year of account that too much had been subscribed in this manner the balance was returned to the policy holders as bonuses either by addition to the sums insured or in reduction of future premiums. Apparently in this case there was another class of non-members, i.e., persons holding non-participating policies. There has been some discussion in the later cases as to whether Lord Watson in *Styles'* case (1) intended to find that the insurance company carried on a business; for he says "The corporation, as a branch of its business, dealt in what are termed 'participating' policies, which it issued to all persons, whether members or not, etc." It was contended that in that case the New York Life Insurance Company and its business fell under the decision of the House of Lords in *Last's* case(2). Lord Watson pointed out that in the New York case the policy-holders are not outsiders, because they and they alone were members of the company, and according to the constitution of the latter insurance by means of a participating policy was the only possible qualification for membership, and when that kind of insurance was effected the insured became practically a partner. This, as pointed out by Lord Watson, distinguished it from *Last's* case(2). Lord Watson further thought that when a number of persons agree to contribute funds for a common purpose, and to stipulate that their contributions so far as not required for that purpose shall be repaid to them they should not be regarded as traders and that the contributions returned to them should not be regarded as profits. Lord Bramwell, who was the dissenting Judge of the three in the House of Lords in *Last's* case(2), after observing that the company was a corporation but that made no difference (a fact which is pointed out in several of the cases noted below) added that the argument was that there were no persons outside the associated members from whom an income is derived and therefore there can be no profit. He was of opinion that the New York Case was not governed by *Last's* case and that the principle of the decision in this case was that there was a company making profits not from its own members but from those it dealt with and that though it returned two-thirds of these profits to those it dealt with, they were none the less profits and therefore income-tax was payable. The learned Lord thought that that decision was wrong. But as he points out, in the New York case there is one body only, the assured, who are not dealing with another body and are not to make profits but to insure themselves and each other on terms as low as can be consistent with safety and solvency. Lord Merschell also regarded the fact that the society was incorporated as immaterial and agreed

(1) 2 Tax Cas. 460, 14 App. Cas. 381.

(2) 2 Tax Cas. 400; 10 App. Cas. 438.

with the majority in *Last's* case that the so-called profits must be examined to see if they really are so or not, because moneys which are not in fact profits if erroneously so-called would not make them profits under the Income-tax Act. Lord Macnaghten also points out the difference between the *New York* case and *Last's*. In the latter case, the insured were not members of the corporation which was formed to carry on a business which had for its object the acquisition of gain by the corporation itself as well as by the individual members. It was a trading concern.

As has been often pointed out, you cannot make a profit out of trading with yourself; so, if in the present case the distributions under Rule 20 are only a return to the members of the Society of the notional price in excess of the actual cost of production—whether you call it paying interest or payment of a dividend in proportion to purchases made—that in my opinion would bring this case within the ambit of *Styles'* case. But, of course, if the payment of interest on the share capital is not such a return but is a distribution of profits in the sense of paying a dividend within the ordinary meaning of the term as applied to a dividend paying company then it is clearly outside the principle of the *Styles'* case and would fall within the principle of the *Last's* case (*infra.*) and perhaps several of the others. That brings us to *Last v. London Assurance Corporation* (1), which was a singularly unfortunate case, if one may say so, because there seems to have been a difference of opinion right through. In the Queen's Bench Division Day, J., and A. L. Smith, J., held different views. In the Court of Appeal Brett, M.R., and Cotton, L.J., affirmed Day, J.'s opinion, Lindley L.J., dissenting. When the case got to the House of Lords, of the three learned Lords, Lord Blackburn and Lord Fitzgerald reversed the Court of Appeal against the opinion of Lord Bramwell; so as was pointed out in a later case four Judges were one way and four the other.

In *Last's* case the Company issued participating policies at an increased premium and at the end of every five years the gross profits of these policies were dealt with by returning two-thirds by way of bonus or abatement of premiums to the holders of the policies, the remaining one-third going to the company, who bore the whole expenses of the business, the portion remaining after payment of expenses constituting the only profit available for division amongst shareholders. Lord Bramwell was of opinion that the difficulty had arisen from the inaccurate use of the expression "participation in profits" for which he would substitute "participation in the sum that would be profits but for the right to participate." Lord Blackburn found himself unable to agree in the error he thought ran through the judgments of all three Judges from whom he differed, namely, that no share in profits can by bargain be given by a company to anyone who is not a shareholder. The principle of this decision has been more than once explained in *Styles'* and other cases so that further comment on the opinion delivered seems to be unnecessary.

The distinction between the two leading cases is very clearly pointed out in *Equitable Life Assurance Society of United States v. Bishop* (2). There it was held that the surplus returned or credited to the policy-holders was "annual profits or gains." As pointed by Darling, J., there was an independent distinct body—the company—as contrasted with the policy-holders and this distinguished it from *Styles'* case. The learned Judge also held that the Equitable Society was not a mutual undertaking pure and simple and that therefore the case fell under the principle of *Last's* case on the ground of the existence of two distinct

(1) 2 Tax Cas. 100; 10 App. Cas. 438.

(2) 4 Tax Cas. 147; (1900) 1 Q. B. 177.

bodies as indicated. The same case went up to the Court of Appeal, where the decision of the Divisional Court was upheld and there it was clearly laid down by Vaughan Williams, J., that the fact that the Equitable Society was incorporated made no difference whatever. He said "The mere fact that the relationship of the parties interested in this business was worked out by the machinery of an incorporated company does not make any difference whatsoever." The learned Lord Justice goes to point out the difference between *Last's* case and *Styles'* case; "In the former the machinery of the company was not used only for the purpose of distributing, in reduction of the cost of insurance, the surplus of the receipts beyond the expenditure, but one-third of such surplus was handed over as profits. In *Styles'* case there was no such dealing with any part of the surplus whatsoever. The whole of the surplus was appropriated to the reduction of the cost of insurance. In the present case it is not true to say that the whole of the surplus is used in the reduction of the cost of insurance because there is some of it paid to the share-holders of the company who are entirely different people from the members of the mutual insurance body."

If one may say so, that puts in a nutshell the difference between *Last's* case and *Styles'* case and the reason for including the Equitable case in the former and not in the latter category.

The Commissioner does not seem to have been very happy in basing his decision on the *Liverpool Corn Trade Association Ltd. v. Monks*(1), because in that case it is clear that there were not only members of the Association who were required to be shareholders in the Company but there were also subscribers. The Company appears to have been of the nature of a club confined to persons interested in the corn trade. The most part of its receipts were derived from entrance fees and subscriptions paid by members. There were various facilities provided for such as desired to make use of them, the subscriptions paid by members being less than those payable by outsiders. The case did not go further than the King's Bench Division where Mr. Justice Rowlatt decided that the profits which the Company made out of what the members paid to it was taxable income of the business which the company undoubtedly carried. The learned Judge regarded as profits the difference which is obtained by dealings between the corporation and the persons who happen to be its members. *Styles'* case was relied on for the assessee but was not accepted by the learned Judge. The facts which seem to have impressed the Judge were that the association was a company with share capital and shareholders with the right to dividends if and when declared on the share capital; that dealings took place by the company with the persons who happened to be the owners of the share capital; and that benefits were afforded to persons individually for which they paid by way of subscriptions and entrance fees.

Thomas v. Richard Evans & Co.(2) was a case of a colliery company which was a member of an association, a company limited by guarantee, formed to indemnify its members against compensation payable in respect of fatal accidents to their workmen. Calls were made by the association and paid by the members for insurance. Out of these a general fund was built up to meet claims for indemnity. A reserve fund was also created the interest on which might go in diminution of the calls upon members. It was held that *Styles'* case applied. There again Rowlatt, J., observed that: "if the people were to do the thing for themselves there would be no profit, and the fact that they incorporate a legal entity to do it for them makes no difference, there is still no profit as the money is collected from those people and handed back to them, not in the character of

(1) 10 Tax Cas. 442; (1926) 2 K. B. 170.

(2) (1927) 1 K. B. 33.

shareholders, but in the character of those who have paid it," this being the principle of *Styles'* case. In the Court of Appeal, the same view was held, namely, that it was a mutual insurance company of associated colliery owners who insured in the association of which they were all members, against their liability to pay compensation to workmen. Scrutton, L.J., observes that the question had been raised as to what exactly was decided in *Styles'* case whether the House of Lords decided that a mutual insurance company did not trade with its members (and he referred to the sentence of Lord Watson quoted above) or whether they decided that the result of its trading with its members was not a profit. The learned Lord Justice also points out that in the *Cornish Mutual Case*(1) the House of Lords held that it was not decided in *Styles'* case that a mutual insurance company did not trade with its members, but that what was decided was that the profits which it made and the return to its members were not profits assessable to income-tax, and that this must now be taken to be the *ratio decidendi* in *Styles'* case.

Thomas v. Richard Evans & Co.(2) went to the House of Lords, where the decision of the Court of Appeal was affirmed on the ground that the Association did not make a profit out of the contributions of the policy holders. It is again pointed out that incorporation makes no difference. The decision is based on the ground that sooner or later the whole of the company's receipts must go back to the policy holders as a class.

The *Cornish Mutual case*(1), which the Crown strongly relied in the present case was a question of corporation tax and the point agitated seems to have been as to whether a corporation, as in *Styles'* case carried on a trade or not. This case is also referred to in *Thomas v. Richard Evans*(2), as construing the judgment of the House of Lords in *Styles'* case and as deciding that such an association did carry on a trade with its members but that the resulting profits of such a trade were not assessable to income-tax. The two questions are obviously different and the sole question in the *Cornish Mutual* case as stated by Viscount Cave, L.C., was whether the company was carrying on a trade or business. I do not think it is disputed in the present case that the Society does carry on a trade or business in Southern India and in fact Rule 2 (a) sets out that the object of the society is to carry on "the business of planters, growers, producers, merchants.....and any other trade or business, etc." and the Crown relies upon the last phrase in the paragraph "any other trade or business which may seem calculated to conduce to the more efficient or profitable working of the said business" and the adjective "profitable" is seized upon as indicating the making of profits. As is pointed out by Lord Herschell in *Styles'* case calling something "profits" will not make it so. It may very well be argued that "profitable working" means advantageous working or working in the best way to further the interests of the society. We must also bear in mind that the important matter in the present case is to discover how the profits are *derived*—not how they are distributed. Some comment has been made on the remarks of Rowlatt, J., in *Thomas v. Richard Evans & Co.*(2), and in the *Liverpool Corn Trade Association v. Monks*(3), cases decided by him on successive days—in both of which he uses the illustration of a railway company or any other concern, trading with its own shareholders. He says the profit made therefrom is exactly the same as if it had been derived from strangers, the profit belongs to the shareholders in a sense, but does not come back to them as purchasers or customers. Of course, a shareholder properly so-called is not a partner with the company in which he is a share-holder. The policy-holders in *Styles'* case were held to be practically in the position of

(1) (1926) A. C. 281.

(2) 11 Tax Cas. 790; (1927) A. C. 827.

(3) 10 Tax Cas. 442.

partners and this may be the distinction. Whatever it be, there can be no doubt as has been held by the highest authority that there are in this connection two groups of cases—those falling under the principle of *Last's case* and other similar cases on the one hand and those falling under the principle of *Styles' case* on the other.

The only other case referred to was the *Commissioners of Inland Revenue v. The Sparkford Vale Co-operative Society Ltd.* (1). That was a case of corporation tax under section 53 of the Finance Act of 1921. The rules provided for a division of profits of five per cent. as a first charge on the net profits. It was held that, although the society bought milk from its own members, sales of milk were made to the outside public and the profits of the society were derived from these sales and were therefore taxable. The question as to whether the fact of the existence of a rule providing for the payment of a dividend (as in this case) took it out of the category of co-operative societies was not raised, but it is very significant that in the statement of the case in the report it does appear that this figures prominently in the rules and was set out in the case submitted for the opinion of the High Court.

If therefore this return of interest on the share capital to the persons called shareholders, namely, the Co-operative Wholesale Society and the Scottish Co-operative Wholesale Society, is simply, as it appears to be and as is sworn by the affidavit of Sir Fairless Barber, merely a return on the amount of its subscribed capital or a handing back of a portion of the amount subscribed and in no sense a dividend on the profits earned by the Company, then I think it falls within the ambit of *Styles' case*; and if this is so, it is simply a return in another form of the rateable dividend in Rule 20 (e). It is clearly not a division of profits in the ordinary sense but is purely notional, for we are told that no money changes hands. This notional profit is calculated on the difference between the market price of the commodities at the time they are distributed to the members of this Society and the actual cost of their production to the Society when ascertained. This so-called profit is distributed in the six ways provided for in Rule 20 and on this so-called profit after allowing for depreciation, interest is to be paid on the share capital, i.e., to the only two members of the Society in proportion to their contributions to the capital. I am unable to see on the facts of this case as disclosed in the rules and on the only evidence we have, namely, the affidavit of Sir Fairless Barber, any evidence of a profit being made by sales to persons outside the membership of the Society. There is no evidence as stated above that any other societies except the two named in Rule 5 have been admitted to membership. It seems to me that this is a case of a purely mutual concern. We know that the whole of the produce raised and exported by the association is in fact divided among these two members.

I am therefore of opinion that the appellants are a purely mutual co-operative society making no profits and therefore not liable to income-tax in this country.

CHIEF JUSTICE:—Having regard to the considerable sum of money involved, it is probable that this case may not end here but will go to the Privy Council. As it is concerned with two subject-matters of which the Indian Courts have a very limited experience, namely, income-tax and the legal position of Co-operative Societies, I think it best to state the position as it presents itself to me as briefly as possible.

The Company with which we are concerned was incorporated in England on the 31st December 1923, under the Industrial and Provident Societies Act of

(1) 12 Tax Cas. 891.

1893. It has not been sought to have it registered, and it has not been registered as a co-operative society in India. Before its incorporation there existed two large Co-operative Societies in Great Britain, one in England known as the Wholesale Co-operative Society, Ltd., and the other in Scotland known as the Scottish Co-operative Society, Ltd. They were co-operative societies of the familiar type which deliver goods to their members on a system the object of which is to eliminate the profits of the middleman as between those societies and their individual members. The goods they were to distribute to their members the Societies had of course to purchase in the market. A portion of the goods so distributed were products of Southern India, notably tea. The idea then occurred that a further elimination of outside profits could be effected by producing their own tea and other products. Accordingly the Corporation now sought to be assessed was founded with the object of acquiring and working estates in various parts of the world including Southern India to supply the two original Co-operative Societies with the goods they required direct. The English and Scottish Co-operative Society, Ltd., was limited by guarantee and the number of shares was unlimited, the capital being stated to be £2,400,000. A tea estate as is well-known yields a certain amount of low grade tea which it would not be worth while to export to the United Kingdom and other perishable goods unfit for transport. These the Society sold locally, the alternative being to throw them away. Certain profits have been derived from these sales and the Society does not dispute its liability to pay income-tax in India on that profit. But it was so negligible a fraction of the whole of the tea and other products grown by it that no one would venture to suggest—and it has not been suggested that that small factor should determine this case. In fact the only shareholders in the English and Scottish Society are the two original Co-operative Societies registered in England and Scotland respectively and the object of the Society sought to be assessed is simply to run the estates, grow the produce required and ship it to the two component Societies which are its share-holders. The produce is invoiced to these two shareholders at a figure which represents the market price for the moment, less the cost of production. The contention for the Crown is that the cost so debited to the shareholding Societies by the “apex” Society as it is called is to be regarded as taxable profits in the hands of the latter. We have had cited to us all the leading English cases on the subject. Unfortunately there is no decision of the Privy Council which would resolve all our difficulties. The discussion narrowed itself in the end to putting it to us in this form: does this case fall within *Last’s* case(1), or *Styles’* case(2). The other cases were treated mainly as explanatory of how the dividing line between those governing cases is to be found.

I have had the advantage of perusing the judgment prepared by my brother Odgers and I have come to the conclusion that he is right in regarding this as a case of a genuine Co-operative Society and therefore immune from income-tax. The Society cannot make taxable profits out of its own component elements, and, with that starting point established, it is to my mind immaterial that the monies that come into the hands of the apex society are distributed in the form in part of a dividend to the shareholders so long as those shareholders do not include any person or body who is not a member of the Co-operative Society. It is quite clear on the facts as stated that that is so in this case. I was at one time impressed by the fact that the component bodies who form the shareholders and the only shareholders in the English and Scottish Society received a dividend of 6 per cent.; but I think it clear on the facts that that was only an anticipatory return to them of what they themselves had contributed and, as the shareholders were component members of the apex society, that could only be regarded as a means of returning

(1) 2 Tax Cas. 100.

(2) 2 Tax Cas. 460.

to them in part money which was throughout treated as theirs and due to be returned to them. If these are not taxable profits when received, the method of returning them to those who contributed them is a matter of internal machinery with which we are not concerned. For myself I only desire to add this to the reasoning of Odgers, J., with which I entirely concur, that I think the case for the Crown relied too much on possible constructions of the rules of the Society which, I will assume for the purpose of the argument, might enable them to conduct their business otherwise than on a strictly co-operative basis. It appears to me that, when we are considering whether there exists or does not exist a taxable income, we are concerned not with whether it is possible for the Society within the meaning of its rules to receive taxable profits but whether in the year of assessment they have in fact received such profits and I am completely satisfied that they have not.

We fix the cost to be paid by the Crown at Rs. 500.

BEASLEY, J.:—I agree.

(289) IN THE HIGH COURT OF JUDICATURE AT RANGOON.

*Before Sir Guy Rutledge, Kt., Chief Justice, Mr. Justice Carr and
Mr. Justice Brown.*

(18th February, 1929).

Chan I.o Chwan and Tong Hock Hin

.. Assessee.*

v.

The Commissioner of Income-tax, Burma

.. Referring Officer.

Income-tax Act (XI of 1922), Secs. 13, & 23 (2)—Accounts rejected as not genuine—Non-disclosure of grounds therefor to assessee—Asst. on insufficient materials, legality of.

Where the assessee's accounts are found not genuine, the Income-tax Officer is under no obligation either in law or in common fairness to set out to the assessee all the reasons therefor and can proceed to make an assessment upon materials, albeit insufficient, without giving notice of his dissatisfaction to the assessee under Sec. 23 (2) of the Income-tax Act.

Case [Civil Misc. Application No. 13 of 1928], stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Burma, for the opinion of the High Court.

CASE. [Civil Misc. App. 13 of 1928.]

In compliance with the order of the High Court of Judicature at Rangoon in Civil Miscellaneous Case No. 13 of 1928, I state a case in respect of the following points of law:—"Can an Income-tax Officer, having rejected the accounts of an assessee as not being genuine, proceed to make an assessment (i) on insufficient material, and (ii) without giving notice of his dissatisfaction to the assessee under section 23 (2) of the Act?"

2. The main point of this case appears to be that the Income-tax Officer came to the conclusion that the books produced were not genuine and made the assessment on the materials available, including the previous years' assessments.

* A. I. R. (1929) Rang. 102.

3. The assessee is a paddy trader and property owner. For the paddy business, he has a number of buying agencies in the district and a head office in Rangoon which he conducts himself. He also arranges for the sale of paddy sent by district dealers and receives brokerage.

4. For the 1922-23 assessment, the assessee declared a profit of Rs. 20,392, but was assessed on the basis of his accounts on an income of Rs. 31,921.

For the 1923-24 assessment, the assessee declared a net loss of Rs. 3,556, claiming a loss of Rs. 50,364 to have occurred in the branch business; but as no accounts of these branch businesses were produced, the loss was not allowed, and the income for assessment was estimated as Rs. 1,02,162. On appeal the figure was reduced to Rs. 93,261.

For the 1924-25 assessment, a loss of Rs. 68,342 was declared, and complete accounts for the head office were produced, but only one unclosed book for each branch. It was alleged that complete accounts were not maintained for the branches; but the Income-tax Officer came to the conclusion that accounts were maintained for the branches but were being withheld; and he made the assessment under section 23 (4). The assessee made an application under section 27, but the Income-tax Officer adhered to his view. On appeal, the appellate officer also held that branch accounts were in existence and declined to interfere. The case came up before the Commissioner on review under section 33 and he also held that the accounts were incomplete and that a book of original entry was most probably withheld. But he reduced the assessment on other grounds by Rs. 38,809 (making the total income Rs. 1,03,852).

For the 1925-26 assessment (the one which is the subject of this reference), the Rangoon office accounts were produced, and also one journal and one ledger for each of the six permanent buying agencies. The results shown in these accounts were entirely inconsistent with the past history of the business and the extent of its operations in the previous year as ascertained by inquiry from various sources. The Income-tax Officer held that the books produced were made up for income-tax purposes and accordingly rejected them and made an assessment on the basis of such data as he could secure.

On appeal, the Assistant Commissioner confirmed the assessment, taking the view that even on the basis of the capital which was admittedly employed in the business it was impossible to hold that the volume of the assessee's business was as small as he claimed it to be. He said "The assessee's capital is Rs. 7,30,000. Even granting that this includes the value of house property, it is clear that no less than Rs. 2,68,650 was borrowed during the year of account. It is impossible to suggest that only Rs. 9,38,618 worth of paddy was purchased during the year with a capital of at least 3 lakhs of rupees. With such a capital about 25 lakhs of rupees worth of business could have been done. Assessee's large borrowing during the accounting year shows that he is not contracting but enlarging his business."

In the application to the Commissioner for a reference to the High Court, the main question was whether there was sufficient justification for the rejection by the Income-tax Officer of the books of account produced by the assessee. My predecessor came to the conclusion that there was plenty of evidence before the Income-tax Officer and in his (my predecessor's) opinion it was incredible that the assessee should be expanding his business if he had made losses for the last three years. And my predecessor also was forced to the conclusion that the accounts were not genuine. In a business of this magnitude, there can be no doubt that proper and fuller accounts were maintained for the branch purchases.

5. As regards the first part of the question at issue, the relevant provisions of the Act are contained in sections 13 and 23. Section 13 provides that the method of accounting regularly employed by the assessee should be adopted for the purpose of computing the income, subject to the proviso that, if no method of accounting has been regularly employed, or if the method employed is such that, in the opinion of the Income-tax Officer, the income cannot properly be deduced therefrom, then the computation shall be made upon such basis and in such manner as the Income-tax Officer may determine. The position is that, even where there are accounts available for the assessment, the law allows the Income-tax Officer discretion in the matter of accepting or rejecting those accounts. Where, as in the present case, accounts are rejected as spurious, the position is the same as if there were no accounts at all and therefore the Income-tax Officer is authorised to make the assessment upon such basis and in such manner as he may determine. Turning to section 23, which deals with the making of an assessment, sub-section (1) of this section provides that, if a return made is correct and complete, the assessment shall be made on the basis of such return. Where the return is incorrect or incomplete, the assessment is made under section 23 (3) after considering such evidence as the assessee may offer in support of his return. Where no valid return is filed, or where there is any default in the matter of producing accounts under section 22 (4), or in the matter of complying with requisitions under section 23 (2), the law [section 23 (4)] directs the Income-tax Officer to make the assessment to the best of his judgment. Whether acting under section 23 (3) or under section 23 (4), an Income-tax Officer may have—and in a large number of cases actually has—to make the assessment on sufficient materials; but whether the materials are insufficient or not the law requires him to make an assessment. In this connection, I would invite a reference to the remarks of Lord Mackenzie in *Macpherson & Co. v. Moore*(1). “if the Act of Parliament says the amount of profits is to be ascertained, ascertained they must be whether that can be done in a satisfactory method or not,” and to the remarks of the Lord President in the same case “Messrs. Macpherson & Co., who if they don’t choose as they have not chosen, to state an account so that the amount of profits may be strictly determined, cannot complain if a random assessment is made upon them by the Crown.” In my opinion, therefore, the first part of the question should be answered in the affirmative.

6. The reply to the second question, in my opinion, is to be found in sub-sections (2) and (3) of section 23. If the Income-tax Officer has reason to believe that a return is incorrect or incomplete, he must serve on the assessee a notice requiring him either to attend or to produce any evidence on which he may rely in support of the return. And after hearing such evidence as the assessee may produce and such other evidence as the officer may require on specified points, he must make the assessment.

I find from the proceedings that two notices were issued under section 23 (2) and also an informal notice requiring the assessee’s attendance. The assessee was examined on two occasions and his statements were recorded. But he was not questioned on the specific points which formed the grounds for the officer rejecting the accounts.

In my opinion, there is nothing in the Act specifically requiring an Income-tax Officer to inform the assessee of his grounds for discrediting his accounts or other evidence. Therefore, it is not legally incumbent on the Income-tax Officer to do so and consequently his failure to do so cannot invalidate the assessment. Under departmental instructions the Income-tax Officer ought to

(1) 6 Tax. Cas. 107 at p. 115.

have given the assessee an opportunity of meeting his criticisms of the accounts. But the case did not depend on these objections, for there were other indications that the accounts were spurious, as pointed out above. The Assistant Commissioner came to the same opinion on the admitted figure of the capital employed in the business.

7. In the questions which the assessee asked the Commissioner to refer to the High Court, I am of opinion that, eliminating the matter of the discrepancies, there was no question of law which could not be answered by a re-statement of the sections above mentioned.

CASE. [Civil Reference 11 of 1928.]

Case [Civil Reference No. 11 of 1928], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Burma, for the opinion of the High Court.

The following reference is made under the provisions of section 66 (2) of the Indian Income-tax Act on the application of Messrs. Tong Hock Hin of No. 49, Strand Road, Rangoon, in respect of their assessment for the year 1927-28.

2. The main point involved is the question of the rejection as spurious of the accounts produced by the firm for the 1927-28 assessment and the determination of their income on an estimate basis. For a proper appreciation of the point at issue it is necessary to state the history of the assessee's assessments for previous years.

3. The assessee is a rice-miller and rice merchant. They have their head office at Rangoon and their rice-mills in the Tharrawaddy District. They are also owners of house-property.

For the 1924-25 assessment, the assessee returned a loss from business of Rs. 1,86,270. This loss was claimed to have occurred in connection with speculation in rice. No details were given in the accounts produced. Losses in respect of various contracts were shown in lump sums. There were no purchase or sales notes. While these accounts could not be checked or relied upon in any degree, the Income-tax Officer found that it was true that the firm did not do good business in the relevant accounting year and accordingly accepted the position that no profits were made. The income from house-property amounting to Rs. 29,103 was taxed, no set-off being allowed as the loss claimed in respect of business was not proved.

For the 1925-26 assessment, the assessee declared a loss of Rs. 5,216. The accounts which were produced, however, showed that there was no loss, but they were so incomplete and faulty that no reliance whatever could be placed on them. There were no sales accounts for the business carried on with rice merchants in the Straits. Certain payments made to the assessee by other Chinese firms on account of interest on loans advanced by the assessee were not shown in the assessee's Interest Account, although an Interest Account was maintained. These payments were not denied by the assessee. There was no Consignment Account showing the consignments received from the firm's mills in the Tharrawaddy District. In short, the accounts were so incomplete and also so demonstrably false in parts that they had to be rejected

and the income determined on an estimate basis. The figures of income adopted were as follows:—

Rs.	1,20,000	from Business.
Rs.	40,000	from Interest on loans made by the firm.
Rs.	40,836	from Property.
Rs.	1,211	from Other Sources.
<hr/>		
Rs.	2,02,047	
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For the 1926-27 assessment, the firm returned an income of Rs. 95,912, the income from business being returned as Rs. 63,638. On the basis of the accounts produced, however, the income of the business was found to be Rs. 79,576, that is. after adding certain items which should have been added back for income-tax purposes. Here again, the accounts were found to be incomplete and faulty to a degree which indicated that they were *ad hoc* productions prepared for income-tax purposes. Sales were shewn at abnormally low rates. Another fact which went to prove that the accounts were untrustworthy was that whereas the accounts of another assessee showed a purchase from this concern of rice at Rs. 522-8 per 100 baskets, not a single transaction in the assessee's accounts showed a transaction at that rate, the rates shewn in the assessee's books being markedly lower. The assessee was asked to trace the particular sale in their accounts. They were unable to trace the transaction though their own Sales Note in respect of it was made available to them, nor were they able to offer any explanation in regard to the omission. This definitely proved the accounts to be false and they were accordingly rejected. The profits from the business were computed at Rs. 2,00,000 and the profits from the loans made by the firm at Rs. 60,000. The income from property was determined as Rs. 41,287. Total Rs. 3,01,287. There was an appeal to the Assistant Commissioner. The appellate officer upheld the action of the Income-tax Officer in rejecting the accounts for the purpose of assessment, but reduced the assessment by a sum of Rs. 13,149 on other grounds.

4. For the 1927-28 assessment, the assessment now in question, the assessee returned an income of Rs. 65,947, being Rs. 38,929 from business and Rs. 27,018 from house-property. The head-office accounts and the accounts of the mills at Tharrawaddy were produced. These accounts also were found to be unsatisfactory, and the assessee was called upon to supply explanations in respect of several discrepancies and omissions noticed by the Income-tax Officer. They or their representatives were summoned for this purpose on six occasions and such explanations as they had to offer in regard to both the incompleteness of the accounts and the particular errors noticed in them were recorded. Finally, the Income-tax Officer rejected the accounts as unreliable for the reasons specified in the assessment order (Exhibit A) and made the assessment, as in previous years, on an estimate basis, the income determined being Rs. 2,25,000 from business and Rs. 60,000 from interest. The assessee's figure for income from property was accepted. On appeal, the Assistant Commissioner reduced the income from business by Rs. 25,000, but confirmed the action of the Income-tax Officer in rejecting the accounts. The Assistant Commissioner held that the probable conclusion from the nature of the errors and omissions in the accounts was that they had been concocted for income-tax purposes. He further noted that, even if such shewn a manner that no use whatever could be made of them. (A copy of his order is attached as Exhibit B.*).

* Not printed.

5. The two questions which I am asked to refer to the High Court are reproduced below :—

- (i) Whether an estimated assessment of an arbitrary nature on insufficient evidence can in law be made in petitioner's case without any details to show how the amount determined upon was arrived at?
- (ii) Whether after the accounts had been rejected an assessee should not be given a chance after due notice to explain the accounts put forward?

6. The first question cannot be referred in the terms stated inasmuch as it assumes that the assessment was made on an arbitrary basis. The question, which can be said to arise, is:—

Whether an assessment can, in the circumstances of this case, that is, where the accounts are rejected as untrustworthy, be made on insufficient materials and whether in such case it is incumbent on the assessing officer to set out the exact details of his computation?

The answer to this question will be found in section 13 of the Act. The proviso to this section enacts:—

Provided that, if no method of accounting has been regularly employed, or if the method employed is such that, in the opinion of the Income-tax Officer, the income, profits and gains cannot properly be deduced therefrom, then the computation shall be made upon such basis and in such manner as the Income-tax Officer may determine.

In the present case the income could not be determined on the basis of the accounts produced by the assessee and so the Income-tax Officer acting in accordance with the said proviso computed it on the available materials including past assessments and his knowledge of similar businesses and of this business in particular. There is no provision in this section or in any other section of the Act requiring the Income-tax Officer to give details of his computation. The position is that whether materials are insufficient or not the law requires the Income-tax Officer to make an assessment. In this connection, I would invite a reference to the remarks of Lord Mackenzie in *Macpherson & Co. v. Moore* (6 Tax Cases, page 115):—

If the Act of Parliament says the amount of profits is to be ascertained, ascertained they must be whether that can be done in a satisfactory method or not.

and to the remarks of the Lord President in the same case (*ibid*, page 114):—

Messrs. Macpherson & Co., who, if they do not choose, as they have not chosen, to state an account so that the amount of profits may be strictly determined, cannot complain if a random assessment is made upon them by the Crown.

In my opinion, therefore, the first part of the question, as reconstructed, should be answered in the affirmative and the latter part in the negative.

7. The reply to the second question, in my opinion, is to be found in subsections (2) and (3) of section 23. If the Income-tax Officer has reason to believe that a return is incorrect or incomplete, he must serve on the assessee a notice requiring him either to attend or to produce any evidence on which he may rely in support of the return. And, after hearing such evidence as the assessee may produce and such other evidence as the officer may require on

specified points, he must make the assessment. As has been indicated in paragraph 4 above, no less than six notices were issued under section 23 (2) to the assessee. The assessee or their representatives were examined on six occasions and their statements recorded. In the course of these appearances and examinations it was made abundantly clear to the assessee and their representatives that the accounts were regarded as incomplete and unreliable and they were asked for explanations as regards the omissions and errors on which the Income-tax Officer based that conclusion.

So much for the facts. The legal position, however, is that there is nothing in the Act specifically requiring an Income-tax Officer to inform the assessee of his grounds for discrediting his accounts or other evidence and that therefore it is not legally incumbent on the Income-tax Officer to do so. Consequently, even if there had been failure to do so, such failure would not invalidate the assessment. In my opinion, therefore, this question should be answered in the negative.

Cowasjee and Daniel, for the Assessee.

Government Advocate, for the Crown.

JUDGMENT (Civil Misc. App. 13 of 1928.)

In compliance with an order of this Bench in Civil Miscellaneous Case No. 13 of 1928, the Commissioner of Income-tax, Burma, has stated a case on the following points of law:—Can an Income-tax Officer having rejected the accounts of an assessee as not being genuine, proceed to make an assessment (i) on insufficient material and (ii) without giving notice of his dissatisfaction to the assessee under section 23 (2) of the Act?

In his statement of the case, the Commissioner reviews the circumstances attending the assessment of the present respondent since the year 1922-23. From this, it appears that the accounts at any rate since the year 1924-25 have been rejected as incomplete and fraudulent, and merely made up for income-tax purposes. The Commissioner sets out the grounds on which the income-tax authorities were satisfied that the statement of accounts was incomplete and fraudulent and we consider that they had good grounds for forming such an opinion. Whether the statement is incomplete and fraudulent or not is a question of fact for the determination of the income-tax authorities and not a question on which this Bench can interfere, and, indeed, from the wording of the reference, this seems to be taken for granted, as it assumes that the Income-tax Officer was within his rights in rejecting the accounts as not being genuine.

The first question then is: Can he proceed to make an assessment on insufficient material? We think on this point the quotations which the Commissioner has made from the case of *MacPherson & Company v. Moore* (1) are very much to the point. In that case, no doubt MacPherson & Company had failed to make any return, but we quite fail to see why a party who has made a false return should be in a better position than one who has failed to make any return. Mr. Cowasjee urges that section 13 only applies to the method and does not empower the Income-tax authority in any way. We cannot see any such limitation in the words of the proviso, which run as follows:—“Provided that if no method of accounting has been regularly employed or if the method employed is such that in the opinion of the Income-tax Officer the income, profits and gains cannot properly be deduced therefrom, then the computation shall be made on such basis and in such manner as the Income-tax Officer may determine.”

In this case, the Income-tax Officer clearly considered that the income, profits and gains could not properly be detected from respondent's statement, since he decided that that statement was not genuine. He was consequently entitled to adopt whatever method he thought best. Adapting the words of the Lord President in *Macpherson's* case already alluded to "If Chan Lo Chwan does not choose to make an honest statement of account so that the amount of profits may be strictly determined, he cannot complain if a random assessment is made upon him by the Crown." For years, according to the Commissioner, the firm has made defective and dishonest returns for the purpose of income-tax and it is to be hoped that it will at last dawn upon them that honesty is the best policy and that this Court will not aid them in reducing the administration of the Income-tax law to a nullity.

The second question in the reference is: Can the Income-tax Officer make an assessment without giving notice of his dissatisfaction to the assessee under section 23 (2) of the Act? On this point, the Commissioner states that two notices were issued under section 23 (2) and also an informal notice requiring the assessee's attendance. The assessee was examined on two occasions and his statements were recorded. He admits that the assessee was not questioned on the specific points which form the grounds for the Officer rejecting the accounts. The controversy on this point seems to come to this: For the assessee it is urged that the Income-tax Officer should give him particulars in respect of the grounds on which he thinks that the statement was not genuine or on which it is incomplete. We may say that there is no such provision in the Act and that the Government Advocate's observation that it was a matter for the legislature rather than the Court seems to be justified. In an ordinary case, we have no hesitation in saying that such particulars ought to be given in a notice, especially in cases where the objection is that the accounts are incomplete. Here, however, where the finding is that the accounts of the assessee in previous years as well as in this year were not genuine but were merely cooked for income-tax purposes, we do not consider that the Income-tax Officer was under any obligation either in law or in common fairness to set out all the reasons which led him to come to such a conclusion.

We accordingly agree with the answers given by the Commissioner in respect of both questions and we order the respondent to pay the Commissioner's costs, 7 gold mohurs.

Foucar, for the Assessee.

Government Advocate, for the Crown.

JUDGMENT (Civil Reference 11 of 1929).

This case is very similar to the one just decided, (Civil Miscellaneous No. 13 of 1928), the only difference being that the questions were referred to this Court by the Commissioner under section 66 (2) of the Act.

The questions referred are:—(1) whether an assessment can in the circumstances of the case, that is, where the accounts are rejected as untrustworthy, be made on insufficient materials and whether it is incumbent on the assessing officer to set out the exact details of his computation?

(2) Whether after the accounts had been rejected an assessee should not be given a chance after due notice to explain the accounts put forward.

The statements of accounts of the assessee for 1924-25, 1925-26, and 1926-27 were rejected on the ground of being false and the same took place for the year 1927-28, which is the assessment now in question. The assessee had no less than six opportunities to explain his accounts or produce any evidence in

support of the return, so that he has, if possible, less merits than the assessee in the previous case.

For the reasons there given, we consider that the Income-tax Officer was fully justified in making the assessment under section 13 of the Act. We agree with the answers given by the Commissioner of Income-tax in his statement of the case and we answer them accordingly. Respondent must pay the Commissioner's costs, 7 gold mohurs.

(290) IN THE HIGH COURT OF JUDICATURE AT PATNA.

Before Mr. Justice Kulwant Sahay and Mr. Justice Fazal Ali.

(19th February, 1929).

Damodar Prasad and others

Assessee.*

v.

The Commissioner of Income-tax, Behar and Orissa. . . Referring Officer.

Income-tax Act (XI of 1922), Sec. 30—Appeal presented unverified and unsigned—Rejection in limine, legality of.

The Assistant Commissioner of Income-tax is entitled to reject in limine an unsigned and unverified appeal petition and there is no provision in the Income-tax Act requiring the Asst. Commissioner to call upon the appellant to rectify the mistakes in the appeal.

Application (Misc. Judicial Case No. 1 of 1929) under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) for an order to direct the Commissioner of Income-tax, Behar and Orissa, to state a case for the opinion of the High Court.

N. K. Prasad, for the Assessee.

C. M. Agarwala, for the Crown.

JUDGMENT.

This is an application under section 66 (3) of the Income-tax Act for an order on the Commissioner to make a reference to this Court on certain points of law set out in the petition. It appears that the petitioner submitted his return under section 22 of the Act on the 23rd August, 1927. Thereupon a notice was issued by the Income-tax Officer under section 22 (4) of the Act directing him to produce certain account books. He produced two account books whereupon he was again ordered to produce certain other books and certain original promissory notes and bonds. The petitioner failed to comply with this requisition and thereupon the Income-tax Officer proceeded to make the assessment under section 23 (4).

The petitioner preferred an appeal to the Assistant Commissioner of Income-tax which was however not in proper form inasmuch as it did not comply with the provisions of rule 21 of the Income-tax rules. The Assistant Commissioner passed the following order on the 2nd December, 1927:—"The petition of appeal does not bear the signature of the appellant and has not been verified in the prescribed manner. It is therefore not admitted. Inform petitioner by p.c." Thereupon he went to the Commissioner with an application to refer the case to this Court. The learned Commissioner has refused to do so on the ground that the only point of law which could arise out of the order of the 2nd December, 1927, was whether the Assistant Commissioner was entitled in law to reject the

* A. I. R. (1929) Pat. 409.

appeal *in limine*. The learned Commissioner says that this question was not formulated by the petitioner under section 66 (2) of the Act, while the two questions which had been formulated by him did not arise out of the appellate order and therefore did not require any discussion. The learned Commissioner, however, did consider the point on the merits and was of opinion that no case had been made out for a reference to the High Court.

The petitioner has now come to this Court for an order upon the Commissioner to make the reference.

It is admitted before us that the petition of appeal before the Assistant Commissioner was not in proper form. Upon that admission it is clear that the Assistant Commissioner was right in refusing to admit the appeal. It is, however, contended that the effect of the order of the Assistant Commissioner was the rejection of the appeal and that the Officer was not entitled to reject the appeal on account of certain defects in the form of the appeal and all that he could do was to call upon the petitioner to rectify the mistakes in the memorandum of appeal. In my opinion there is no provision which requires the Assistant Commissioner to take this step, namely, to call upon the appellant to rectify mistakes in the memorandum of appeal. He did, however, inform the appellant by a post card that the appeal was not admitted on account of certain defects which were pointed out in the card. It was open to the appellant to approach the Assistant Commissioner with a prayer to allow him to rectify the mistakes and if he had done so there is no reason to suppose that the Assistant Commissioner would not have allowed him to do so. As has been pointed out by the learned Commissioner the only point of law which could arise out of the order of the 2nd December, 1927, was not taken before him, and even assuming that the petitioner is entitled to take this point here in this Court we are of opinion that the point is not a good point and cannot prevail.

As regards the merits, it is clear that the matter not having been considered by the Assistant Commissioner it cannot be considered by us here in this Court. It, however, seems to be clear that it was open to the Income-tax Officer under section 22 (4) of the Act to require the petitioner to produce such accounts or documents as the Income-tax Officer thought necessary, and section 23 (4) provides that if the requisition under section 22 (4) is not complied with the Income-tax Officer shall make the assessment to the best of his judgment. There was the requisition under section 22 (4) which was not complied with and, therefore, the assessment made by the Income-tax Officer under section 23 (4) appears to be legal.

This application must be dismissed with costs. Hearing fee three gold mohurs.

(291) IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Mr. Justice L. G. Mukerji and Mr. Justice Niamat Ullah.

(20th February, 1929).

Shiva Prasad Gupta

v.

Assessee.*

The Commissioner of Income-tax, United Provinces

Referring Officer.

Income-tax Act (XI of 1922), Secs. 13 & 66 (3) & (5)—Reference to High Court—Scope and limits of High Court's powers—Jurisdiction, if confined to

questions framed by Commissioner—Assessee taking credit for interest for years previous to account year—Claim to debit losses and irrecoverable debts of those years—Income-tax Officer's powers under Sec. 13.

On an application under Sec. 66 (3) of the Income-tax Act it will be for the High Court to find out what is the point of law that arises and requires decision and what is to be referred to the High Court is the statement of the case or the case itself, not a point or points of law.

Although ordinarily the Commissioner of Income-tax would be the Officer who would frame the points of law that arose in the case stated by him and although he would be expected to give his opinion thereon for the benefit of the High Court, Sec. 66 (5) requires the High Court to decide the questions of law that arise in the case, that is, the High Court is entitled to 'resettle the issues' as it were and decide those issues of law. The duties of the High Court are not confined to answering the question of law put to it by the Commissioner, whether or not such question is a substantial question to be decided between the parties.

Under a partition of joint family properties effected on the 26th February 1926 (1983-S.) to have effect as from 9th October 1921 (1979-S.), the assessee was given as his share certain outstanding debts of the family business. To ascertain his position, the assessee prepared a profit and loss account showing on the credit side the interest accrued during the period 1978-S. to 1983-S. each year being shown separately and on the debit side such amounts as represented either a loss in business or unrealised or irrecoverable debts. On an assessment to income-tax for the year 1927-1928, the Income-tax Officer took all the accumulated interest of the several years (1978-1983) as the assessee's income of the account year 1926-1927 but refused to allow for the losses claimed for those years.

HELD, that the assessee was entitled to deduct the losses and the irrecoverable debts that happened and should have been discovered respectively in the years 1978-1983.

Under Sec. 13 of the Act, the Income-tax Officer has no arbitrary power to assess the income.

Case (Misc. Case No. 1001 of 1928), stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, United Provinces, for the opinion of the High Court.

CASE.

Babu Shiva Prasad Gupta was assessed to income-tax by the Income-tax Officer of Benares on March 10, 1928, on the income received in 1926-27 for an income of Rs. 1,31,786. He preferred an appeal to the Assistant Commissioner of Income-tax of Benares on March 25, 1928. The Assistant Commissioner of Income-tax of Benares partly accepted the appeal and partly rejected it, and held the total income of Babu Shiva Prasad Gupta only Rs. 1,07,753.

2. The facts of the case, as explained in the following passage from the appellate order of the Assistant Commissioner of Income-tax of Benares, dated April 19, 1928, are:—"This firm is the off-shoot of the parent firm of an undivided Hindu family named Sital Prasad Kharag Prasad. The firm of Sital Prasad Kharag Prasad had Hon'ble Raja Hoti Chand, C.I.E., of Azmatgarh Palace, as head or *karta* of the undivided Hindu family. Under mutual agreement the partition of the estate of this undivided Hindu family was made by arbitrators (Pandit Madan Mohan Malaviya and Rai Bahadur Pandit Baldeo Ram Dave). Under this partition Babu Shiva Prasad Gupta is now the sole proprietor of the

firm of Shrijut Balkrishna Das Bisheshwar Prasad, resident of Seva Upavan, Benares."

3. The present reference to the Hon'ble High Court refers to the decision of the Assistant Commissioner of Income-tax of Benares regarding *paragraphs 1 to 8* (appendix A*) of the grounds of appeal preferred to the said Officer by Babu Shiva Prasad Gupta, and it may be better to note below the wordings of the said decision:—

"*Paragraphs 1 to 8.*—The gist of the contention is, that, after the partition had taken place, the appellant worked out his accounts in order to ascertain his position regarding the outstanding balances of debts which were allotted to his share, and that the interests worked out on these outstanding balances of debts were the interests due for previous years for the accrued interest of which the firm of Messrs. Sital Prasad Kharag Prasad had paid tax in those years, and that the accounting done was an ascertainment of the income from interest either on cash basis or on mercantile system. So far as the payment of tax on the accrued interest by the parent firm Messrs. Sital Prasad Kharag Prasad is concerned, I have gone through the assessment records of the past years showing the details of the income reported to Calcutta by the Income-tax Officer of Benares for assessment purposes. I find from these reports of the Income-tax Officer of Benares that never any accrued interest in respect of the outstanding balances of loans was reported by the Income-tax Officer of Benares to the Income-tax Officer of Calcutta. As to the allegation that the accounts were not adjusted and that there was no accounting either on the cash basis or on the mercantile system, I find that the accounts were adjusted and accrued interest was worked out on the mercantile system. Only one instance of a big loan out of the many will show that I am right about my presumption. When the partition allotted certain outstanding balances of loan to Babu Shiva Prasad Gupta, it was found that the Rana of Khajurgaon owed Rs. 3,58,934 as principal sum. The accumulated interest worked out to Rs. 68,065. Thus the total came to Rs. 4,26,999. But the Rana of Khajurgaon having paid over Rs. 65,000, the balance carried over to the next year's account was only Rs. 3,62,000 in round figures. This is, therefore, on mercantile system, and the Income-tax Officer was quite right to include all the accrued interest worked out in this way and added to the principal as the income of the appellant, and I do not accept these contentions. When this view is taken, the contention of the appellant, through his learned vakil is, that, when this is done, the previous years' losses worked out in the same accounts by the appellant, and the bad debts of those years worked out in the same accounts ought to have been allowed as debits. I do not agree with this view. The addition of accumulated interest to the principal sum and carrying over of the whole amount in future years means the realization of that interest in the year when the accounts are adjusted and the accumulated interests are added to the principal. In other words, this accumulated interest is realized in the year when it is adjusted by adding it to the principal. It is not previous year's collection and realization. That analogy, therefore, does not apply to the debits of the previous years' losses and bad debts. The Income-tax Officer has, upon very good grounds, disallowed them; and I do not find any reason to differ from him. The result is that I do not accept the contentions made in paragraphs 1 to 8."

4. Mr. Shiva Prasad Gupta, in his application under section 66 (appendix B*), accepts the Assistant Commissioner's finding that his accounts are maintained on the "mercantile system". (It will be seen later that I do not accept that finding). His contention is, that, according to that system, accumulated interest that has accrued in the course of a series of years is rightly treated as income in any year in which the assessee elects to take credit for it in his accounts, as been

done here. This is not, as a matter of fact, in accordance with the mercantile system of accountancy. Similarly he claims that business losses, bad debts, and that particular class of bad debts which are distinctively known as "irrecoverable loans"—that is, bad debts arising out of money-lending which, under any system of accountancy, include the principal loan, and, under the mercantile system (but not under the cash system) include also any interest that has accrued and for which credit has been taken but that has not been realized—are to be allowed as "expenditure incurred solely for the purpose of earning" the profits or gains to be taxed under section 10 (2) (ix) of the Indian Income-tax Act (there is no other provision of the law under which an allowance on this account can be claimed) whenever the assessee chooses to debit them, or write them off in his accounts. A bare statement of the assessee's theory is sufficient, I think, to suggest that, if it were accepted, an assessee could manipulate his accounts so as to make his assessable income in any given year (within a very large margin) much what it suited him to make it. The income of the previous year would not be determined according to any settled principle of accountancy, nor would it bear any constant relation to facts. It would be determined largely by the mere caprice or convenience of the assessee, or the degree of punctuality with which he wrote up his accounts.

5. In the second of the two clauses of his additional application (appendix C*), the assessee has claimed that the depreciation allowable on the machinery, buildings, etc., of his "Gyan Mandal" press should be allowed against his total joint income from all heads. The direct intention of the provisions in proviso (b) of clause (vi) of sub-section (2) of section 10 is that any excess of depreciation over profits should not be adjusted from other heads of income, but held over for subsequent adjustments in later years when the profits of the plant concerned could carry it. The distinction between depreciation, which is in the nature of a replacement fund, and actual losses to which section 24 (1) would apply is a real and not merely a theoretical one. The fact that a firm has not been able to set aside its legitimate quota towards its machinery replacement funds does not constitute any diminution of its income. A specific remedy is provided that any deficiency in contribution to this replacement fund should be made good by excess allowance in future years. This clearly shows the intention of the legislature to keep the depreciation account solely attached to the plant concerned.

6. The applicant has not definitely formulated the questions that he desires to be referred to your Lordships, but they appear to be the following:—

- (1) In computing the income, profits and gains of the previous year, for the purpose of assessing them to income-tax, can business losses incurred in years anterior to the previous year be set off against income of the previous year?
- (2) Similarly, in computing the income of the previous year, can bad debts or irrecoverable loans that became bad or irrecoverable respectively in years anterior to the previous year be deducted from the income of the previous year?
- (3) If the answer to these two questions be in the negative, can interest that accrued in years anterior to the previous year, but for which the assessee in accordance with the system of accountancy regularly employed by him (see section 13 of the Indian Income-tax Act) has taken credit for the first time in the previous year, be included in computing the income of the previous year for the purpose of assessing it to income-tax?

* Not printed.

7. I am required by the law to give my own opinion in regard to these questions. My replies are as follows:—

Questions 1 and 2.—No. The Act provides that the assessment should be made on the income of the previous year. That income is to be computed in accordance with the system of accountancy regularly employed by the assessee (section 13), provided that the Income-tax Officer is satisfied that the income, profits and gains can be properly deduced therefrom. If he is not so satisfied, the Act gives him the widest discretion as to the manner in which it should be computed.

Whether any system of accountancy has been regularly employed by the assessee, and, if so, what that system is, are both questions of fact to be determined by the assessing authorities. I submit, further, that no question of law can arise in regard to the exercise by those authorities of the discretion vested in them to determine whether the system of accountancy employed by the assessee is such that his income can be properly deduced therefrom, so long as they have adequate materials on which to base a conclusion, apply their minds thereto, and do nothing manifestly contrary to equity or good conscience.

8. On the strength of a report submitted by the Assistant Commissioner of Income-tax after a further examination of the accounts I find that the system of accountancy employed by the assessee, so far as his printing press to which the business loss relates, is the ordinary system of mercantile accountancy. According to that system, sums falling due by or to the business man are debited or credited in the accounts *when they fall due* by him or to him. A “business loss,” according to this system of accountancy, is simply the excess of debits over credits; and if the accounts are correctly and punctually maintained, this loss comes into the business man’s accounts in the year in which the constituent credits and debits accrue. Of course the system of mercantile accountancy—like the law—is *non cogit ad impossibilia*. The profit or loss resulting from a certain transaction may only be ascertained some time after it has actually occurred, and is then properly entered in the accounts when it is ascertained. But no attempt has been made to prove in the present case that in the principles either of any recognized system of accountancy, or of any system of accountancy “regularly employed” (section 13) by the applicant, any justification is to be found for debiting in the accounts of one year expenditure—real or notional—that manifestly relates to another year, and that should and could have been debited in the accounts of that other year. So much for the business loss. The same argument applies to the bad debts, in regard to which I would also invite your Lordships’ attention to the decision of the High Court of Lahore in the case of *Puran Mull v. Commissioner of Income-tax*(1).

9. In regard to the *irrecoverable loans* my conclusion is the same, but the position is slightly different, because the system of accountancy regularly followed by the applicant in his money-lending transactions is not the mercantile system of accountancy, as is evident from the report of the Assistant Commissioner of Income-tax, dated July 19, 1928, an extract from which is annexed to this statement (appendix D.*). I consider that this report justifies my coming to a definite finding of fact on this point. The system of accountancy employed by the applicant for his money-lending is really more nearly akin to the cash than to the mercantile system. Interest that has accrued, but has not been received, is not credited to the accounts until either a decree has been obtained for it, or a fresh document has been executed in which it is added to the original principal. Here we have a clear, if not very scientific, “method of accounting regularly employed” by the applicant, and one by no means unusual in India. If it is followed

* Not printed.

consistently, there is no reason to suppose that, on the average, it is unfair either to the assessee or to the Revenue. Of course, where accrued but not realized, interest is only treated as income when a decree is obtained or a new document is executed, and where even realized interest is only taken into account when accounts are "settled", there would be no objection to "irrecoverable loans" being similarly written off on corresponding occasions. No attempt has been made, however, to show that the writing off in this case is on all fours with the crediting of accrued interest. It is clear that when the applicant came to review what he had got out of the partition of the property of the undivided family, he found amongst his assets a certain proportion of what—to use a homely word—may be described as "duds" that ought to have been written off years ago. There is no reason whatever why, because these long valueless book credits have been unloaded on the applicant as part of his share of the family property, he should now be allowed to deduct them from his income. So far as he is concerned, they represent not even a capital loss, but merely what I may call a capital disappointment.

10. *Question 3.*—My reply is "yes." I have unavoidably anticipated this question in dealing with question 2. Since in accordance with the method of accountancy employed by the assessee in regard to his receipts—method that is not open to serious objection and that the Income-tax Officer has accepted as one from which the income, profits and gains can properly be deduced (section 13)—interest that accrued in years anterior to the accounting period has been credited to the profit ledger for the first time in the "previous year" it has rightly been treated as income of the previous year. If, of course, it were proved that any of this interest had been taken into account in computing the income for assessment in previous years, I should be prepared to admit that, as a matter of commonsense and equity, any such items should be omitted—whatever might be the strict letter of the law. No such claim is advanced. What the applicant says in effect is: "This is income of years anterior to the previous year. According to my system of accountancy it was not treated as income in those years. You accepted that system of accountancy then, and did not tax it then. It now comes into the income of the previous year: according to my system of accountancy, but you must not tax it." This contention is patently repugnant to ordinary common sense, and directly contrary to the provisions of section 13.

11. Paragraphs 1 to 6 of the statement of the case were sent to the petitioner for observations and representation if any and copy of his representation is attached as appendix E.* I do not consider it necessary to make any addition or alteration.

Sir Tej Bahadur Sapru and Ramakant Malaviya, for the Assessee.

Uma Shankar Bajpai, for the Crown.

JUDGMENT.

MUKERJI, J.:—This is a reference by the Commissioner of Income-tax, United Provinces under Sec. 66 of the Income-tax Act of 1922.

The facts as they appear from the statement of the case made by the learned Commissioner and from the several appendices attached to the statement appear to be as follows:—There was a joint family business owned by several members of the family, the head office of which was in Calcutta. The income-tax for the entire business was paid at Calcutta by the head office firm carrying on business under the name and style of Sital Prasad Kharag Prasad. The members of the family decided to separate, as and from the date 9th October 1921. The date of separation having been fixed by mutual agreement, the actual partition of the effects of the family was made over to two gentlemen, Pandit Madan Mohan

* Not printed.

Malaviya and Babu Baldeo Ram Dave. These gentlemen made an award on 30th of November 1925. The said award was made a rule of the court on 26th February 1926. It was, therefore, on 26th February 1926 that the assessee, B. Shiva Prasad Gupta, at whose instance this reference has been made, became the owner of the lot given to him as the result of the partition. 26th February 1926 was almost at the close of the samvat year 1982. The Samvat year 1983 began on 15th of March 1926. For the samvat 1983 B. Shiva Prasad Gupta had a statement of his financial position drawn up in the shape of a profit and loss account. I have already mentioned that the family became separate with effect from 9th October 1921 which would correspond to sometime about Katik 1978 samvat. In preparing the profit and loss account on the credit or income side was shown the interest which accrued to B. Shiva Prasad during the years 1978 samvat to 1983 samvat, each year being shown separately. On the debit or loss side, was shown for different years, such amounts as represented either a loss in business or un-realisable debts.

B. Shiva Prasad Gupta was to be assessed for his income of the year 1927-28. The amount of his probable income, for the purpose of assessment, was to be taken to have been the same as was his actual income in the "previous year", namely 1926-27 which would approximately correspond to the samvat year 1983.

Having the profit and loss account, prepared as aforesaid before him, the Income-tax Officer took all the accumulated interest of the several years as B. Shiva Prasad's income from the year 1926-27. B. Shiva Prasad's contention was that, if on the income side the interest that accumulated from time to time was to be shown as the income of the particular year 1926-27 (samvat 1983), he was entitled to set off, as against that income, the losses suffered by him in business (the main business being a printing press), and on account of irrecoverable debts.

Apparently, the Income-tax Officer refused to deduct, out of the so-called income of B. Shiva Prasad Gupta for the year 1926-27, his losses during the years, the interest earned for which have been taken as his income. There was an appeal to the Asst. Commissioner. It was unsuccessful except in so far as the assessable income was slightly reduced by him.

The assessee petitioned the Income-tax Commissioner to refer his case to the High Court but he did not formulate the questions of law that really arose for decision. The learned Commissioner of Income-tax has formulated three questions for being answered by the High Court. These are as follows:—

- (1) In computing the income, profits and gains of the previous year, for the purpose of assessing them to income-tax, can business losses incurred in years anterior to the previous year be set off against the income of the previous year?
- (2) Similarly, in computing the income of the previous year can bad debts or irrecoverable loans that became bad or irrecoverable respectively in years anterior to the previous year be deducted from the income of the previous year?
- (3) If the answer to these two questions be in the negative, can interest that accrued in years anterior to the previous year, but for which the assessee in accordance with the system of accountancy regularly employed by him (see section 13 of the Indian Income-tax Act) has taken credit for the first time in the previous year, be included in

computing the income of the previous year for the purpose of assessing it to income-tax?

It will be noticed that the first two questions do not really arise in the case. The third question again does not state the actual question that is in controversy. It entirely ignores the contention of Mr. Gupta that he is entitled to deduction out of what has been taken to be his income.

The learned Government Advocate has contended that the High Court has no power to find out for itself what are the substantial questions of law that have arisen between the parties and that it is bound either to answer such questions as have been put to it by the Commissioner of Income-tax, or send back the case to him to make a fresh "statement" in the case.

In view of this contention, I have considered Sec. 66 of the Indian Income-tax Act carefully. I am unable to find any warrant in it for the extreme contention of the learned Government Advocate. It appears to me that the section is not happily worded and the pronoun "it" has been used sometimes for a "question of law" and sometimes for the "case". The meaning and object however of the entire section 66 seems to me to be free from obscurity. My impression is that the High Court has to accept the facts as found by the Commissioner of Income-tax and if necessary may call for more facts by asking him to make a fresh statement of them under sub-section 4 of section 66. But it is for the High Court to find out, from the contention of the assessee on the one hand and the contention of the income-tax authorities on the other, what is the real point of law that arises between the parties and what it has to decide. This reading of Sec. 66 seems to be clear to me, from, among other matters, the fact that the High Court is nowhere called upon to decide such questions as may be framed by the Commissioner of Income-tax.

Let us now read Sec. 66 clause by clause. Sub-section 1 says:—"Where in the course of any assessment a question of law arises, the Commissioner may draw up a statement of the case and refer "it" with his own opinion to the High Court." The pronoun "it" may refer either to the case which word appears close by, or it may refer to the "question" of law which word "question" appears four lines earlier.

Sub-section 2 mentions the case where reference is to be made at the instance of the assessee, sub-section 1 having already provided that a reference could be made by the Income-tax Commissioner either of his own motion, or on reference from any income-tax authority subordinate to him. Here again, the pronoun "it" that appears after the word "refer" may stand for the "case" or the "question" of law. The proviso to sub-section (2) makes it clear that the object of the reference is the decision by the High Court of the question of law that arises in the case and the main object of sending up the "case" is the decision of the question of law. The proviso says that if the Commissioner, in the exercise of his power of revision, decides the "question", which can mean only the question of law that arises, the assessee may withdraw his application for a reference to the High Court. If the assessee is satisfied with the Commissioner's decision on the point of law he may choose that he no longer would have a decision by the High Court.

Sub-rule 3 relates to the position that might arise if the Commissioner happens to be of opinion that there is no question of law to be decided and the High Court is of opinion that there is a question of law to be decided and all that the High Court wants is a statement of the case by the Commissioner. Obviously, in these circumstances, it will be for the High Court to find out what is the point

of law that arises and requires decision. In this sub-section, what is to be referred to the High Court is the statement of the case, or the case itself and not a point or points of law.

Sub-rule 4 relates to the affair when the statement of the case made by the Commissioner is unsatisfactory. It says that where a statement in a case referred under this section (Sec. 66) is insufficient to enable the High Court to determine the question raised "thereby", namely by the case, the court may refer back the case to the Commissioner for additions and alterations. This proviso supports the view that it would be for the High Court to find out what is the real point of law that is in issue between the assessee on the one hand and the income-tax authorities on the other and whether for the purposes of determination of the point of law, sufficient facts have been supplied. It must be remembered that the questions of law that would ordinarily arise would arise in connection with particular facts and must be answered with reference to those facts. Otherwise, there would be no necessity of a statement of a case or any addition or alteration in that statement. It would be sufficient merely to put an abstract question of law to the High Court for an answer.

Sub-rule 5 says that the High Court, on hearing any such "case" shall decide the "question of law raised thereby". The word "thereby" must stand for "the case". This sub-rule nowhere suggests that the duties of the High Court are confined to answering the question of law put to it by the Commissioner whether or not such question is a substantial question that is to be decided between the parties (the assessee and the income-tax authority).

The result of my reading of Sec. 66, therefore, is that although ordinarily the Income-tax Commissioner would be the officer who would frame the points of law that arise in the case stated by him and although he would be expected to give his own opinion on those points of law for the benefit of the High Court, Sec. 66 requires the High Court to decide the questions of law that arise in the case, i.e., the High Court is entitled to "re-settle the issues" as it were, and decide those issues. Of course, the issues would all be on the questions of law.

This being my reading of the provisions of Sec. 66 of the Income-tax Act, I find that the only controversy that does arise between the income-tax authority on the one hand and the assessee on the other, is "Whether the assessee is entitled to deduct from his "income", which is in the shape of interest which has accrued due, not only in the year 1926-27, but in five previous years (going up to samvat 1978, see p. 7, Appendix A), the losses and irrecoverable debts that happened and should have been discovered, respectively, in those years?"

The answer to such a question can be only in the affirmative.

It will be recalled among the members of the joint Hindu family, the date of separation was fixed as 9th October 1921, corresponding to 1978 samvat. For full four years, the partition proceedings dragged on and it was not till the close of samvat 1982 that the assessee came to know what he had got as his share in the joint family property. It has been found that no income-tax was paid on the interest that accrued in the years 1978 to 1982, according to the account books. It is clear that income-tax ought to be paid for those years, but no income-tax can be assessed for the years 1978 to 1982, unless the accumulated interest be taken as a part of the income of the year 1983 (1926 to 1927). Prior to the year 1927-28, the assessee could only have been the joint family. The family did not treat the accrued interest as a part of their profits and did not pay any income-tax on the same. In the profits and loss account, the assessee, Mr. Shiva Prasad Gupta, treated the accumulated interest as his income for the year 1983. This

treatment by Mr. Gupta was only for the purpose of ascertainment of his own financial position. It would be an untrue statement of fact if we said that the accumulated interest of 5 years was Mr. Shiva Prasad's income in one particular year, namely 1983. But he is prepared to allow the income-tax authorities to treat the entire accumulated interest as his income for the "previous year", provided he is allowed to set off against the interest, that accrued in a particular year, the loss that was incurred in the business (press) or due to particular debt becoming irrecoverable, in that particular year. This is a perfectly fair and equitable position and is not in any way discountenanced by Sec. 13 of the Income-tax Act.

Section 13 of the Income-tax Act is a very fair section, if properly understood. It says that when an assessee keeps his accounts in a particular way in order to ascertain his own profit and loss, take his case of profit and loss in his particular way, provided it gives an accurate idea of his income in a particular period. But for this purpose, the method of keeping the account should be one which the assessee habitually and regularly adopts. This can only mean that the practice has gone on for some time. In this particular case before me, there can be no question of any particular method of keeping account which may have been "regularly employed", to quote the exact language of Sec. 13. Mr. Gupta came by his separate property in the very year under consideration, viz., 1926-27. He could not possibly have developed for himself any method of accounting as to which the description "regularly employed" may be applied. The Income-tax Officer, in the circumstances, is thrown upon "such basis" and "such manner" as the Income-tax Officer may determine; see Sec. 13. This does not mean that the Income-tax Officer has a purely arbitrary power to assess the income. If he adopts one particular method he is to pursue it to its logical conclusion. In this case, the Income-tax Officer adopts the assessee's 'chitta' or profit and loss account for the purposes of Sec. 13 of the Income-tax Act, but he accepts only the figures on the one side and ignores the figures on the other. In other words he proceeds on what has been described in the course of the argument and in the statement of the case as "mercantile accountancy system." That system is this. In any particular year, the amounts that have become recoverable are shown as the income actually received and the liabilities incurred are shown as amounts actually disbursed. Under this system, the merchant, in order to ascertain his income, which is really a "book income", deducts from the profit earned according to his books, the losses that he has suffered, also according to his books. The balance is a net 'book income'. Under Sec. 13 of the Income-tax Act, this net 'book income' may be accepted by the Income-tax Officer as a fair estimate of the merchant's income. The reason will be two-fold. The merchant himself uses this method of ascertaining his own income and, secondly the method is not an unfair one. In this particular case before me, the Income-tax Officer accepts the 'book income' of any particular year, say for example, the year 1979 as the assessee's income, because the assessee, in his 'profit and loss account' has taken the book income of 1979 samvat as his income. But when the assessee ascertained also his losses for the year 1979 in order to ascertain his actual book income for 1979 samvat, the Income-tax Officer says, "you ought to have done that in the year 1979 and you cannot do it now". The simple and honest answer to that would be, "In the year 1979, the accrued interest was never treated as a part of the income and therefore the accrued losses were never deducted out of the income." To my mind, it is manifestly unjust that in treating the book income as the actual income, the losses, which would have been deducted if the book income had been treated as the actual income in a particular year by the assessee, should not be deducted.

My answer to the question formulated above, therefore is that the assessee is entitled to have deducted from his estimated income the actual losses that may

have been suffered in a particular year and the amount of irrecoverable debts that should have been discovered and could have been discovered in a particular year.

As regards the questions put by the learned Commissioner of Income-tax, my simple answer is that those questions do not at all arise, for there is no difference of opinion between him and the assessee on these points. The learned counsel for the assessee, Sir Tej Bahadur Sapru agreed before us, without any difficulty, that the answers to the questions 1 & 2 should be in the negative and the Income-tax Commissioner has himself given his answers to those questions in the negative. As regards the third question, as I have already stated, it does not cover the point in controversy which is, whether or not the assessee is entitled to have deducted from his estimated income certain particular amounts. I need not repeat, therefore, that none of the three questions framed by the learned Commissioner arise in the case. There is no occasion for calling for a fresh statement of the case, under sub-section 4 of Sec. 66, for all the facts necessary for the determination of the real controversy, on the question of law, do appear from the statement of the case furnished to us by the learned Commissioner.

NIAMAT ULLAH, J.:—I concur.

By the COURT:

The question that arises in the case as stated by the learned Commissioner is that indicated in the judgment of one of us and is "Whether the assessee is entitled to deduct from his income which is in the shape of interest which has accrued to him, not only in year 1926 to 1927 but in five previous years (going up to Samvat 1978, see p. 7, Appendix A), the losses and irrecoverable debts that happened and should have been discovered respectively in those years."

Our answer is that to be found in the judgment of one of us namely, "The assessee is entitled to have deducted from his estimated income not only losses that may have been suffered in a particular year and the amount of irrecoverable debts that should have been discovered and could have been discovered in a particular year."

Let a copy of our judgment be sent down to the Commissioner of Income-tax for his information. We certify that the Government Advocate is entitled to a day's fee namely Rs. 200. The costs of this reference shall be paid by the Government. The Government Advocate will have one month's time to certify, as allowed by the rules.

(292) IN THE HIGH COURT OF JUDICATURE AT RANGOON.

Before Mr. Justice Heald and Mr. Justice Otter.

(25th February, 1929).

L. R. M. S. T. Firm

Assessees.

v.

The Commissioner of Income-tax, Burma.

Income-tax Act (XI of 1922), Sec. 66 (3)—Money lending business—Alleged investment of Stridhanam of assessee's female relatives—Interest thereon, claim for deduction—Assessment in Madras as ladies' separate properties—Disallowance of claim—Question, if one of law.

The assessee doing money lending business in Burma on an assessment to income-tax claimed deduction in respect of a sum of Rs. 6,070 as interest on 'investments' of Stridhanam monies of their female relatives in Madras and in support thereof filed affidavits of the ladies and the assessment order on the sums in question as the separate properties of the ladies. On the claim being disallowed an application was put in under Sec. 66 (3) of the Income-tax Act for a reference to the High Court.

HELD, that the fact that an assessment was made in Madras would not prevent the Income-tax Officer in Burma on proper enquiries from coming to the conclusion that the sum in dispute was assessable there, as the surplus investments of the assessee and hence no question of law arose for a reference to court.

Application [Civil Misc. App. No. 167 of 1928] under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) for an order to direct the Commissioner of Income-tax, Burma to state a case for the opinion of the High Court.

Foucar, for the Assessee.

Gaunt, for the Crown.

JUDGMENT.

This is an application for a mandamus to be directed to the Commissioner of Income-tax ordering him to state a case in accordance with the provisions of section 66 (3) of the Indian Income-tax Act of 1922.

The short facts are that the Income-tax Officer of Pegu assessed the applicants for the year 1924-25 to income-tax on a sum of Rs. 6,070, which had escaped assessment. The applicants are a Chettyar firm and for the year 1924-25, the interest on certain "investments" in the firm was allowed to be deducted from the firm's gross profits. This deduction was allowed upon the ground that the said sum was interest on certain stridhanam monies invested in the applicants' business by certain lady relatives of theirs in Madras. The Income-tax Officer had reason to believe that these monies were in fact surplus investments of the partners. He issued notice under sections 34 and 22 (2) of the Act to enhance the original assessment, and the assessment was enhanced. Upon appeal to the Assistant Commissioner, this Officer held that the sum of Rs. 6,070 was assessable to income-tax as part of the income of the applicants' firm and dismissed the appeal.

In support of their contention, the applicants filed affidavits of the ladies in question, and also relied on the fact that the said sum had been assessed for income-tax in Madras as being the separate property of the ladies we have referred to.

It is said that a question of law arises in this case, but we are unable to agree that this is so. The only question is whether the amount under review in fact is interest on funds of the applicants' firm. If it is, it is liable to income-tax in Burma. The fact that there has been an assessment by an Income-tax Officer elsewhere is no doubt a fact to be taken into consideration but it is not conclusive. It appears that the Madras assessment was made upon the statements of the ladies concerned and moreover we observe that the tax paid by the ladies has been allowed for (as an act of grace) in the assessment of the applicants' income. In any event, the fact that the Madras assessment was made would not in our opinion prevent an Income-tax Officer here, after proper enquiry, from coming to the conclusion that the sum assessed was in fact assessable in this Province. If that were not so, the door would be open to fraud on the part of persons who might

get themselves assessed in one place upon one basis, whereas in truth and in fact the assessment should be made in another place upon an entirely different basis. We are not satisfied that any question of law arises and we dismiss the application with costs, advocate's fee to be three gold mohurs.

(293) IN THE HIGH COURT OF JUDICATURE AT PATNA.

Before Mr. Justice Kulwant Sahay and Mr. Justice Fazal Ali.

(11th March, 1929).

Jangi Bhagat Ramawatar

Assessee.*

v.

The Commissioner of Income-tax, Behar and Orissa.

Income-tax Act (XI of 1922), Secs. 22 (4), 23 (4), 28 and 66 (2)—Denial of accounts called for—Assessment on non-production, legality of—Penalty levied by Commissioner under Sec. 28—Application for reference, if lies—Jurisdiction on facts.

An original order passed by the Commissioner under Sec. 28 of the Income-tax Act imposing a penalty does not come within the provisions of Sec. 66 (2), so as to empower the High Court to call upon the Commissioner to state a case thereon.

In an application under Sec. 66 (3) of the Act, it is not open to the Court to go into the facts of the case and to determine whether the Commissioner was right in his findings on the facts.

Service of an order under Sec. 22 (4), upon the Gumastha of the assessee, who produced certain account books before the Income-tax Officer is sufficient compliance with the provisions of law regarding service of notice.

Mere denial of the existence of the account books called for under Sec. 22 (4) will not make their non-production cease to be a failure to comply with the terms of the notice entailing an assessment under Sec. 23 (4).

Application (Misc. Judicial Case No. 18 of 1929), under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) for an order to direct the Commissioner of Income-tax, Behar and Orissa, to state a case for the decision of the High Court.

S. N. Basu and Hiralal Das Gupta, for the Assessee.

C. M. Agarwala, for the Crown.

JUDGMENT.

KULWANT SAHAY, J.:—This is an application under section 66 of the Indian Income-tax Act praying that the Commissioner of Income-tax, Bihar and Orissa, may be required to state a case and to refer it to this Court on the following points:—

- (1) Whether the assessment under section 23 (4) of the Act was valid?
- (2) Whether the order under section 28 of the Act was legal and valid?

- (3) Has there been a misdirection in arriving at a finding about the genuineness or otherwise of the account books produced by the petitioner in as much as the fact that the rokar bears the Income-tax Officer's signature dated 7-10-25 was completely ignored, and if so, whether the finding itself is legal?

The petitioner submits that these points arise under the following circumstances:—

The petitioner has a money lending business at Baldarwa and a rice mill at Adapur in the district of Champaran. The present assessment is for the year 1927-28 which is based on the income of the previous year, the accounting year of the assessee ending in the month of Kartik of the Fasali year. In compliance with a notice under section 22 (2) of the Act he submitted a return showing an assessable income of Rs. 5,787. Thereupon the Income-tax Officer, by his order dated the 21st of December 1926, called upon the assessee to produce accounts in support of the return, and a combined notice under sections 22 (4) and 23 (2) was issued requiring him to produce accounts of the year 1331, 1332 and 1333 Fasli, fixing the 13th of January 1927 for the purpose. On the 13th of January time was granted to the assessee on his application up to the 26th of January. On the 26th of January he produced his account books which were partly examined on that date. On the 27th of January the Income-tax Officer discovered that the account books produced were different from the books which were shown to him when he had gone to the locality on a local inquiry on the 30th July 1926 and which books he says he had signed there on that date. It appears from the order of the Commissioner that the Income-tax Officer had examined the books at Adapur on the 30th of July 1926 and had made notes thereof in the departmental note book kept by the Income-tax Officer and the reference about his visit to the assessee's mill was also found in the Income-tax Officer's diary of the 30th of July 1926.

The Income-tax Officer on examining the books produced before him discovered that there were discrepancies as regards the amount of sale price of rice as shown in the books produced and the sale price noted by him during his local inspection on the 30th July. On the 27th of January, therefore, he made a note in the order-sheet to the effect that the account books produced were different from those signed by him at the time of the local enquiry as the sales did not agree and the assessee was asked under section 22 (4) to produce the books which the Income-tax Officer had signed giving a warning to the assessee that otherwise he will make a heavy assessment and also a penal assessment. The 29th of January was fixed to produce these books. It appears that on the 29th of January a servant of the assessee, named Ibadat Mian, appeared, and it appears from the order-sheet that a petition was filed on that date for a month's time on the ground of illness of the proprietor. The order-sheet shows that the Income-tax Officer was of opinion that the time was asked for simply to evade producing the account books. He, however, allowed another opportunity to the assessee to produce the books and fixed the 31st of January 1927. It is represented that Ibadat Mian at first made an oral application for a short adjournment but that the Income-tax Officer required him to file a written petition praying for a month's time. This the Income-tax Officer denies. He only admits that at first an oral application was made and the Income-tax Officer directed a written application to be filed but he states that he did not direct him to apply for a month's adjournment. It may be noted that the books were produced on the 26th of January 1927 by a gomashtha of the assessee, named Chhathu Lal, and it is contended that Ibadat Mian had no authority to make the application as he was merely a peon and not a gomashtha of the assessee.

On the 31st of January the order sheet shows that Ramautar Prasad the son of the assessee, Jangi Bhagat, both of whom form members of an undivided Hindu family appeared before the Income-tax Officer and stated that the books which the Officer had signed at the mill were not found even after long search and that they were missing. The Income-tax Officer was of opinion that this was a false excuse and he made an assessment on that date under section 23 (4) of the Act on a total income of Rs. 18,350. On the 29th of January the Income-tax Officer also recorded an order on the order-sheet directing the representative of the assessee, namely, Ibadat Mian to show cause on the date fixed, viz., the 31st of January, why penalty under section 28 should not be imposed for deliberately showing a lesser amount as the income from sale of rice. On the 23rd of February 1927, the assessee filed an application before the Income-tax Officer for cancellation of the assessment and for making a fresh assessment under the provisions of section 27 of the Act. The Income-tax Officer rejected this application by his order dated the 4th of June of 1927 and on the same day he imposed a penalty of Rs. 679-5-0 under section 28 of the Act.

The assessee preferred an appeal before the Assistant Commissioner under section 30 of the Act; but this appeal was not admitted by the Assistant Commissioner as in his view the appeal was filed beyond the period of limitation of thirty days provided by sub-section 2 of the section 30 of the Act. The assessee then went before the Commissioner with an application under section 33 of the Act as well as an application under section 66. The learned Commissioner by his order dated 22nd July 1928, held that the assessment under section 23 (4) was legal and proper; but as regards the penalty under section 28, he was of opinion that the procedure adopted by the Income-tax Officer was irregular inasmuch as the order passed by him on the 29th of January, calling upon the representative to show cause why the penalty should not be imposed, was not properly communicated to the assessee, it being signed by Ibadat who was merely a peon and could hardly be held to be an agent of the assessee, and that it was not clear to the Commissioner whether the assessee had in reality an opportunity of showing cause why the penalty should not be imposed. He accordingly cancelled the order; but, as he was doubtful whether the Income-tax Officer had jurisdiction at that stage to take up the matter again, he himself called on the assessee to show cause why a penalty should not be imposed under section 28 on the ground that he had deliberately furnished inaccurate particulars of income and had thereby returned it below its real amount. Ultimately the Commissioner, by his order dated the 6th of November 1928, imposed a penalty of Rs. 6,790. The present application is directed against these two orders dated the 22nd of July 1928 and the 6th November 1928, passed by the Commissioner.

In dealing with the present application this Court is bound to accept the findings of fact arrived at by the Commissioner. It is not open to this Court to go into the facts of the case and to determine whether the Commissioner was right in his findings on the facts. The finding of facts of the Commissioner is that the Income-tax Officer did, as a matter of fact, go to the mill at Adapur on the 30th of July 1926, inspected certain books, made notes in the departmental note-book and in his diary, and signed the books which he had inspected. The Commissioner was also of opinion that the books produced by the assessee on the 29th of January through his gomashtha, Chhothu Lal, were not the real books, and that the Income-tax Officer acted within jurisdiction in issuing the notice on that date calling upon the assessee to produce the account-books which he had signed and the non-compliance with that order gave jurisdiction to the Income-tax Officer to make the assessment under Sec. 23 (4) of the Act. Upon these findings the first and the third point stated in the application now before us, upon which we are asked to require the Commissioner to state a case, do not arise.

It is contended on behalf of the petitioner that the assessment under section 23 (4) was illegal because notice of the order of the 27th of January 1927 was not served personally upon the assessee; that the notice was bad because it did not comply with the provisions of section 22 (4); and that if the assessee is directed to produce account-books which the assessee says were not in existence then the non-production of the books did not amount to a non-compliance of the notice under section 22 (4). In my opinion none of these grounds can prevail. Chhotu Lal appears to be the accredited agent of the assessee; he was the gomastha and produced the books before the Income-tax Officer; and a notice of the order of the 27th of January served upon him was a sufficient compliance with the provisions of the law as regards the service of notice. Nothing is shown why the notice is said not to comply with the provisions of section 22 (4), and the mere fact of the denial of the existence of the account-books required to be produced does not absolve the assessee when it is found upon evidence that the books were really in existence, and the non-production thereof did amount to a failure to comply with the notice under section 22 (4).

As regards the order of the Commissioner imposing the penalty under Sec. 28 of the Act, it is contended by Mr. Agarwala on behalf of the Commissioner that this was an original order passed by the Commissioner and did not come within the provisions of sub-section 3 of section 66 of the Act which would empower this Court to call upon him to state a case. It is contended that it is only against orders passed on appeal under section 31 or 32 of the Act that a reference can be made to this Court by the Commissioner and this Court can not call upon the Commissioner to state a case in respect of orders passed by him not in appeal but as an original order. The petitioner, however, refers to the case of *Sachchidananda Sinha v. The Commissioner of Income-tax*(1). In that case there was an order made by the Commissioner under section 33 of the Act and the Commissioner was required to state a case and ultimately this Court was of opinion that the procedure adopted by the Commissioner was illegal. It does not, however, appear from the decision of that case that the question was raised whether this Court had jurisdiction to act under section 66 of the Act in respect of an original order made by the Commissioner. In a later case, however, in *Trikamjee Jiwan Das v. The Commissioner of Income-tax, Bihar and Orissa*(2), grave doubts were expressed whether the High Court was justified in requiring the Commissioner to state a case. The plain language of section 66 does not empower this Court to require the Commissioner to state a case in respect of an original order passed by him and not in respect of an order passed in a matter which came before him on an appellate order by the Assistant Commissioner. I am, therefore, of opinion that the point No. 2 also does not arise in the present case.

This application is dismissed with costs three gold mohurs.

FAZL ALI, J.:—I agree.

(294) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Justice Sir C. V. Kumaraswami Sastriar, Mr. Justice Odgers and
Mr. Justice Wallace.

(14th March, 1929).

S. V. L. L. Lakshmanan Chettiar

.. Assessee.*

v.

The Commissioner of Income-tax, Madras

.. Referring Officer.

Income-tax Act (XI of 1922), Sec. 4 (1)—*Tavanai loans to persons outside British India—Interest due but not credited in accounts—Assessability.*

(1) 1 I. T. C. 352.

(2) 1 I. T. C. 406.

* (1930) 57 M. L. J. 60; 30 L. W. 82; A. I. R. 1929 Mad. 675.

Interest fallen due but not credited in the account year in respect of Tavanai loans advanced in the course of the assessee's money lending business in British India to persons outside British India is assessable under Sec. 4 (1) of the Income-tax Act as income accruing, arising or received in British India.

Case [O. P. No. 126 of 1928], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

CASE.

I have the honour to refer the following case for the opinion of the Hon'ble the Judges of the High Court under section 66 (2) of the Income-tax Act, 1922.

2. The petitioner is a Nattukottai Chetti resident at Devakottai in the Ramnad District, within the jurisdiction of the Income-tax Officer, First Circle, Karaikudi. He carries on a money lending business at Devakottai and is a partner in some other firms in British India.

3. For the assessment of the year 1927-28 based on the accounts of the Tamil year Akshaya (1926-27), the petitioner returned an income of Rs. 3,430 from his business at Devakottai. The Income-tax Officer who examined his accounts found that he had not taken credit for the interest that had fallen due in the year of account on loans advanced by him to members of his own community on what is known as the *Tavanai* system. The interest on such loans due by persons in British India amounted to Rs. 2,241 and that due by customers in Ceylon and the Straits Settlements amounted to Rs. 5,578. The Income-tax Officer added these as well as other items omitted by the petitioner and fixed the taxable income of the business at Devakottai at Rs. 13,658.

4. The petitioner appealed to the Assistant Commissioner objecting to the assessment of the sum of Rs. 5,578 on the ground that the interest on sums lent to persons in Ceylon and the Straits Settlements accrued and arose outside British India and that it could not be taxed as income unless and until it was actually received in British India. The Assistant Commissioner overruled his objection and upheld the assessment.

5. The petitioner has required me under section 66 (2) of the Income-tax Act to refer certain questions of law for the decision of the High Court. The question arising on the facts of the case is the following and I refer it for the opinion of the High Court:—"Whether the sum of Rs. 5,578 can be taxed under section 4 of the Income-tax Act as income accruing, or arising, or received in British India during the year of account, Akshaya."

6. The loans in question were advanced in the course of the petitioner's business at Devakottai and it is not disputed that they are repayable in British India. The interest on such loans is not a profit or gain arising without British India as has already been held by the Madras High Court in the case of *A. T. K. P. L. S. P. Subramaniam Chettiar v. Commissioner of Income-tax, Madras*(1).

7. The next question is whether the petitioner can be said to have received the interest on these loans during the year of account. The distinguishing feature of *Tavanai* loans is that at the close of each period the interest due, if payment in cash has not been demanded by the creditor, is added on to the principal sum lent, becomes merged in it, and begins to bear interest as part of such principal sums. In effect, therefore, the interest is received at the close of each period and lent again to the original borrower and the receipt should be exhibited as such

even in an account maintained on a cash basis, i.e., as a record of actual receipt. The fact that the creditor did not make the necessary adjustment in his accounts at the end of each *Tavanai*, cannot alter the nature of the transaction. The sum of Rs. 5,578 represented interest for *Tavanai* which fell within the year of account and must be taken to have been received as it became due. It will be noted that the Income-tax Officer included in the assessment the interest due on *Tavanai* loans advanced to persons in British India even though the petitioner had not shown it as a receipt during the year of account and that the petitioner did not at any stage object to this procedure. The fact that the loans in question were made to persons outside British India does not alter the position. I am therefore of opinion that the Income-tax Officer rightly taxed the sum of Rs. 5,578 as income received in the year of *Akshaya*.

R. Kesava Iyengar, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

The petitioner is a Nattukottai merchant residing at Devakotta in the Ramnad District, where he carries on a money lending business. In the course of the business he lent moneys to persons in Ceylon and Straits Settlements on what is known as the *Tavanai* system. The Income-tax Officer assessed the petitioner on the footing that interest in respect of such loans must be taken into account in assessing the petitioner for the year *Akshaya*. Objection was taken that interest on sums lent to persons outside British India cannot be taxed as income arising within British India unless and until they are received in or brought into British India and that as the petitioner did not actually receive interest on the loans he could not be taxed simply because he was getting compound interest. These objections were overruled but on the request of the petitioner the following question was referred to us for decision:—"Whether the sum of Rs. 5,578 can be taxed under section 4 of the Income-tax Act as income accruing, or arising, or received in British India during the year of account, *Akshaya*".

It was asserted by the petitioner during the enquiry before the Income-tax Officer that the moneys were lent on the ordinary *Tavanai* system and we must take it that the usual incidents of loan with an agreement to pay *Tavanai* interest apply. Under such a system interest is agreed to be paid at certain periods and in default of such payment interest remaining unpaid becomes part of the principal and the whole sum carries interest at the rate agreed upon. Debits and credits are made in the accounts on this footing and the amount is carried forward at the end of each *Tavanai* period. The effect is that at the end of each *Tavanai* period the interest due and unpaid at the end of each *Tavanai* is treated as having been received and added to the principal and re-lent on the rate of *Tavanai* interest agreed upon. In *Narayanan Chetti v. Subbiah Chetty* (1), it was held by Wallis, C.J., and Krishnan, J., that in such cases interest unpaid and added to the principal is to be treated as a fresh deposit. In *T. P. Pethaperumal Chettiar v. Commissioner of Income-tax, Madras* (2), which was a reference under the Income-tax Act, Coutts Trotter, C. J., Beasley and Mackay, J., were of opinion that under a loan on *Tavanai* contract at the close of each period the interest due, if payment in cash has not been demanded or paid, is added to the principal sum lent and becomes merged in it and begins to bear interest as part of such principal; that means that interest is to be treated as having been paid and received and is added to the deposit itself to carry interest. We may in this connection also refer to the observations of Napier, J., and Krishnan, J., in

(1) (1920) 43 Mad. 629.

(2) 3 I. T. C. 378.

The Secretary to the Board of Revenue v. Arunachalam(1), at pages 88, 89 as to when interest will, though not actually received, be deemed to have been received. Reference has been made by petitioner's Advocate to the *Secretary to the Board of Revenue v. Pyda Venkatachalapathy*(2), but that case went on the ground that there was nothing in the documents or evidence to show that there was any discharge of the interest due, or constructive receipt of the sum. We are of opinion that the petitioner must for the purpose of assessment to income-tax be deemed to have received interest though it was not actually paid in cash.

The next question is whether he received it in British India within the meaning of section 4 of the Income-tax Act. Under section 4 profits and gains of a business accruing or arising without British India to a person resident in British India shall, if they are received in or brought into British India, be deemed to have accrued or arisen in British India and to be profits and gains of the year in which they are so received and brought. The explanation is to the effect that the mere fact that such profits are taken into account in the balance sheet prepared in British India will not bring the case within this section.

In *Subramanyam Chettiar v. Commissioner of Income-tax, Madras*(3), it was held that where a person who adopted the mercantile basis in his accounts and who carried on business in Rangoon and Penang advanced a sum of money from the Rangoon funds to the Penang business and credited interest on the advance in the Rangoon business though no amount was actually received from Penang, the interest in question was not profit or gain arising outside British India but was income which properly accrued or arose within British India within section 4 (1) of the Income-tax Act. Mr. Kesava Iyengar for the petitioner wanted to canvass the correctness of this decision but we see no ground to dissent from the view taken by the learned Judges.

In the present case it is not suggested that the petitioner was carrying on a separate or a branch business in Colombo and the Straits Settlements. He is a money lender carrying on business in British India and in the course of such business lends money to persons outside British India. It is therefore unnecessary for us to consider the cases cited which had reference to business having branches outside British India.

Reference was made to *Gresham Life Assurance Society v. Bishop*(4), *Farmer v. Scottish Widow's Fund Life Assurance Society*(5), and *Scottish Provident Institution v. Farmer*(6), where it was held that actual receipt of interest or profits is necessary and that a mere inclusion of the amounts in the balance sheet or accounts is not sufficient to make income received in foreign countries taxable. The explanation to section 4 embodies the rule laid down in the decisions cited. In the present case we are of opinion that the explanation to section 4 has no application as for the reasons given by us we think that there has been a receipt of the interest.

We are of opinion that the petitioner has been rightly assessed and answer the reference in the affirmative. The assessee will pay the Income-tax Commissioner's costs Rs. 250.

(1) 1 I. T. C. 75.

(2) 1 I. T. C. 185.

(3) 2 I. T. C. 365.

(4) 4 Tax Cas. 464; (1902) A. C. 287.

(5) 5 Tax Cas. 502.

(6) 6 Tax Cas. 34

(295) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

*Before Justice Sir C. V. Kumaraswami Sastriar, Kt., Mr. Justice Odgers and
Mr. Justice Wallace.*

(15th March, 1929)

A. S. P. L. V. R. Ramaswami Chettiar

Assessee.

v.

The Commissioner of Income-tax, Madras

.. Referring Officer.

Income-tax Act (XI of 1922), Secs. 4 (2) and 2 (1) (xi)—Profits of foreign business in "previous year"—Losses in prior years—If adjustable against profits of "previous year"—Agency accounts not closed and profits ascertained—Assessment under Sec. 4 (2), Legality of.

On an assessment of a sum of money under Sec. 4 (2) of the Income-tax Act as a remittance of foreign profits in 1925-1926, the assessee contended that the foreign business sustained losses in 1922-23-24 and 2' the three years preceding the account year, which if taken into account would leave no available profits in 1925-26 and that further the three years agency accounts of the foreign partnership had not been closed and the assessee's share of profits ascertained, the last closing being in 1921-1922. The Income-tax authorities found that the losses could have been met out of the profits earned prior to 1922-1923 and hence could not be adjusted against the profits earned in 1925-1926 and that the non-ascertainment of the foreign profits would not operate as an exemption from taxation. On a reference to the High Court,

HELD, that there being nothing in the Income-tax Act requiring the taking of accounts of preceding years anterior to the "previous year", the profits of "the previous year" would not cease to be profits of that year on account of losses in prior years and that the assessment was rightly made.

Case [O. P. No. 128 of 1928], stated under Sec. 66 (2) of the Indian Income-tax Act, (XI of 1922), by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

CASE.

I have the honour to refer the following case for the opinion of the Hon'ble the Judges of the High Court under section 66 (2) of the Indian Income-tax Act.

The applicant is a Nattukottai Chetti residing at Pudukkottai in the Ramnad District within the jurisdiction of the Income-tax Officer, I Circle, Karaikudi. He has a money lending business at Kemmendine in Burma and is a partner with a 7/8th share in a firm at Kuala Lumpur in the Federated Malay States. During the year 1925-26 a sum of one lakh of rupees was remitted by the firm at Kuala Lumpur to the shop at Kemmendine. The Income-tax Officer computed the profits of the Kuala Lumpur firm in that year to be \$50,528 and the applicant's share to be \$45,755 or Rs. 70,747. He proposed to tax the sum of Rs. 70,747 as profits of the Kuala Lumpur business remitted to the applicant in British India, under section 4 (2) of the Income-tax Act.

The applicant objected to the proposal on the following among other grounds:—(1) that the firm at Kuala Lumpur sustained a loss during the period of four years ended 1925-26 and there were therefore no profits that could be taxed under section 4 (2). and

(2) that as the accounts of the firm had not been closed within the above period and the profits ascertained and apportioned among the partners, any remittance to one of the partners could not be considered to have been made out of his share of profits in that period. The Income-tax Officer overruled the objections and taxed the applicant on the above sum of Rs. 70,747. The applicant appealed to the Assistant Commissioner without success. A copy of the Assistant Commissioner's order is appended—Ex. A.* The applicant has required me under section 66 (2) of the Income-tax Act to refer certain questions of law for the decision of the High Court. I refer the following questions with my own opinions thereon.

Question 1 (a). Whether the construction put on section 4 (2) by the Assistant Commissioner is correct. (b) Whether the prohibition against setting off losses sustained in previous years against profits of the succeeding year applies to a foreign business. The question briefly appears to be whether the Income-tax Act requires that in calculating the amount of foreign profits available for remittance the Income-tax Officer should take into consideration the aggregate result of four years' trading. I can find nothing in section 4 (2) to warrant this construction. The scheme of the Act is to levy a tax from a person on the income he derives each year and to take no account of the loss he sustained in a previous year. I do not think that the provisions of section 4 (2) create an exception to this general rule. The clause only provides that the profits of a foreign business which accrued or arose in a previous year and which are remitted to British India shall under certain conditions be deemed to have accrued or arisen in British India in the year in which they are remitted. In the present case the applicant had profits in the year of account 1925-26 in his Kuala Lumpur firm. It is not his contention, nor has he proved, that these profits had been applied towards meeting previous losses and were not therefore available for remittance. His profits earned in the years prior to 1922-23 were considerable and these could have been used to cover the losses of the subsequent years. If the applicant's accounts had been closed every year these losses would have been adjusted against his capital or earlier profits and the question of adjusting them against the profits of 1925-26 would not have arisen at all. I am of opinion that the Assistant Commissioner's construction of section 4 (2) is correct and that the losses of years prior to 1925-26 were rightly ignored in the computation of profits available for remittance in that year.

Question 2. Whether the Income-tax Act negatives the custom of Chettys of closing their foreign accounts at the termination of each agency and determining their profits on the closing of those accounts. The Income-tax Act does not "negative" the custom of Chettys in the matter of closing their accounts at any time and determining their profits for any period. The Act requires that a person should be taxed on his annual profits and gains and these profits have to be determined in whatever manner his accounts are maintained. The suggestion seems to be that as the business at Kuala Lumpur is conducted by a partnership and as the profits of that business were not ascertained and apportioned among the partners, the remittances made to the applicant who was one of the partners should not have been treated as a remittance out of his share of profit. In my opinion this contention has no force. In this case there was nothing to prevent the applicant from drawing on the profits of the firm during the period of the partnership. When a remittance was made and there was no proof that it came out of capital it was assumed that it came out of his share of profits. The fact that the partners did not for their own purposes determine their share of profits cannot operate to exempt those profits from taxation. If the business were in British India the profits of the firm would have been ascertained each year and taxed (if otherwise taxable) though the firm had not closed its accounts

and determined its profits every year. The fact that the partnership in this case is outside British India makes no difference.

R. Kesava Iyengar, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.*

This reference arises from the following facts:—The assessee was carrying on business in British India and at Kuala Lumpur, Federated Malay States. In the year of accounting which was 1925-26, a sum of lakh of rupees was sent to the assessee from Kuala Lumpur into British India. The Income-tax authorities found as a fact that out of this sum of a lakh of rupees a sum of rupees 70,000 represented the profits made in Kuala Lumpur during the accounting year of 1925-26 and acting under section 4 (2) they assessed him on that amount. The case for the assessee is that so far as the business in Kuala Lumpur was concerned it was conducted by agents who ordinarily had a three years agency, that in Kuala Lumpur the last agency closed in the years 1921-22, when there was a settlement of account and that till the end of the year of accounting 1925-26 the accounts were not closed, nor was any profit ascertained. It was also contended that during the years 1922-23-24 there was loss in the business and it is argued that the Commissioner was wrong in confining himself to the profits made in 1925-26, that he should have taken the account of the business from the periods 1922-23-24 and 25 and that if such an account was taken there would be no profits. It was also contended that in any event he was bound to take the accounts for the three preceding years and reference is made to section 4 which states that profits which are not brought into British India within three years are not liable to taxation. We must take the facts as found by the Commissioner to be that when an account was taken of the business in 1925-26 it was found that there was a profit of Rs. 70,000 available to be sent to British India as profits.

The question now before us is, whether for purposes of section 4 (2) we must take the profits of the year of accounting and treat the money remitted into British India as taxable, or whether we should go back and take the accounts of the three preceding years or any period anterior to that. This will depend upon the construction of section 4 read with sections 3 and 2 (1) (xi). Section 4 (2) runs as follows:—"Profits and gains of business accruing or arising without British India to a person resident in British India, shall if they are received in or brought into British India, be deemed to have accrued or arisen in British India and to be profits and gains of the year in which they are so received or brought, notwithstanding the fact that they did not so accrue or arise in that year, provided that they are so received or brought in within three years of the end of the year in which they accrued or arose." Section 3 states that the assessment shall be in respect of all income, profits and gains of the previous year of every individual, Hindu undivided family, company, firm and other association of individuals. Section 2 (1) (xi) defines what is meant by "the previous year."

We think that having regard to these provisions all that is necessary to be determined is, whether the money brought into British India was profit that accrued during the year in which it was so brought, or it was profit within three years of the end of the year in which they accrued or arose. There is nothing in the Act which requires us to hold that any account is to be taken of any previous year or years. Ordinarily in British India when accounts are taken they are taken only of the previous year although there may be terms in the partnership that accounts are to be taken of periods exceeding one year. Although no

* Delivered by Kumaramaia Sastri, J.

accounts have been taken for several years it is not open to an assessee in Madras to say that although in the year of accounting there were some profits they should be set off against the loss during the preceding years. The contention that is raised with regard to foreign profits is that though the money was brought into British India in the year of accounting yet it should not be assessed as profits but that an account ought to be taken of the past years. What we are concerned with is, profits for the year as defined in section 2 (11) and it does not cease to be profits of that year because there were losses in the previous years. It is stated that there were losses between 1922 and the year of accounting but there is no reason why such losses should not have been met out of the profits of 1922 not remitted into British India. What we have got is the finding of the Commissioner that the profits made in 1922 were enough to cover the loss incurred in the subsequent years and that in the year of accounting there was a sum of Rs. 70,000 made as profits and available for remittance into British India. The presumption of law is that if there are profits available for remittance into British India it is to be presumed that the moneys so remitted are the profits and not the capital. It is further presumed that where profits have been made before three years, and also profits made within that period, the sums remitted to British India in the year of accounting, are profits made within these three years (see *Scottish Provident Institution v. Allen*(1) and *S. K. R. S. L. Firm v. Commissioner of Income-tax, Madras*(2)).

Having regard to the facts found by the Commissioner of Income-tax, we think that the assessee was rightly assessed on the Rs. 70,000 as profits made during the year of accounting. We answer the reference accordingly. The assessee will pay Rs. 250 as costs of the reference.

(296) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Justice Sir C. V. Kumaraswami Sastriar, Kt., Mr. Justice Odgers and Mr. Justice Wallace.

(15th March, 1929).

Vellanki Lakshmi Narasayamma Rao Bahadur (Sree Raja)

Zamindarini of Tiruvur

.. Assessee.*

v.

The Commissioner of Income-tax, Madras

.. Referring Officer.

Income-tax Act (XI of 1922), Sec. 2 (1)—Maintenance legacy under will of Zamindar—No charge upon immovable properties—If agricultural income.

Under a will executed by the Zamindar of Gunnavaram, the testator appointed his wife as executrix giving her a life interest in the whole of his properties movable and immovable with absolute remainder in favour of his daughters. There was a further provision directing the executrix to pay Rs. 600 per month to each of his daughters in case they desired to live separately. During the year 1924-1925 one of the daughters received from the executrix under a decree of court a sum of Rs. 80,000 being the arrears of the allowance from 1919. On an assessment of this sum, exemption was claimed as agricultural income.

HELD, that the legacy allowance was not agricultural income as defined in Sec. 2 (1) of the Income-tax Act.

(1) 4 Tax Cas. 591 ; (1903) A. C. 129

(2) 2 I. T. C. 359.

* I. L. R. 52 Mad. 827 ; 57 M. L. J. 36 ; 30 L. W. 184 ; A. I. R. (1929) Mad. 598.

Case (O. P. No. 199 of 1928), stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

CASE.

I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (2) of the Indian Income-tax Act, XI of 1922.

2. Sri Raja Vellanki Lakshminarasayamma Rao Garu, Zamindarini of Tiruvur, (hereinafter called the petitioner) objects to an assessment made on her under section 23 (3) of the Income-tax Act for the year commencing on the 1st April 1925 on an income of Rs. 71,254.

3. The facts of the case are:—(a) The petitioner is the daughter of the late Sri Raja Varadaraja Appa Rao Bahadur, Zamindar of Nuzvid and other Zamins (hereinafter referred to as the Testator). The testator owned large moveable and immovable properties. He had no male issue but had two daughters—the petitioner and another, Subbamma Rao Garu.

(b) The testator had no desire to adopt a son nor was he in favour of his wife adopting one. He left three wills dated 26th June 1908, 6th January 1911, and 14th August 1916 (appended as Annexures A,* B,* and C).*

The salient provisions of the wills so far as they are necessary for the purposes of this case were:—

(i) that the whole estate of the testator both movable and immovable over which he had absolute right of enjoyment and the whole movable and immovable estate that might devolve on him in future should after his demise be in the possession and enjoyment of his wife Chellayamma Rao Garu during her life time and that she should have only a life interest therein and not the right to make a gift or effect a mortgage or sale, etc.;

(ii) that after the demise of the wife all the properties should go to his two daughters in equal shares;

(iii) that after the life time of his daughters the properties movable and immovable should devolve on the male issue of the daughters and if they had no male issue, on their female issue and their descendants from generation to generation with absolute right of sale, mortgage or gift, etc.

(iv) that if during the life time of his wife either of his daughters should die without issue the half share of the estate that would devolve on her after the death of his wife, should go to the surviving daughter, and after her demise to her issue;

(v) that if during the life time of his wife both his daughters should die leaving issue, the estate should after her demise go in two equal shares to the issue of his daughters;

(vi) that if at any time during the life time of his wife either of the daughters should desire to live separately from their mother such daughter should be paid by the wife an allowance of Rs. 600 per mensem.

Under this will the testator's wife was appointed the executrix of the will.

4. The petitioner began to live separately from her mother, the widow of the testator. She therefore claimed from the executrix the allowance of Rs. 600 per mensem provided under the will. The executrix apparently con-

* Not printed.

tested the petitioner's right and the latter had to file suits O. S. Nos. 99 of 1919 and O. S. No. 50 of 1922 on the file of the Subordinate Court, Bezwada, to recover the allowances. The Subordinate Judge decreed her claim and during the official year 1924-25 she recovered from the executrix sums aggregating Rs. 83,254-10-9 being the allowance due to her from 1919 plus interest thereon at the rate of 6 per cent per annum.

5. For the assessment of the year 1925-26 the petitioner in response to the notice issued by the Income-tax Officer under section 22 (2) of the Income-tax Act returned this sum of Rs. 83,254 as her income but contended:—(1) that she was not liable to pay any income-tax on this sum as it was paid to her from the agricultural income of an estate which was paying peishush to Government and was therefore exempt from income-tax and (2) that if the receipt was held to be income liable to tax, a sum of Rs. 30,000 being the expenses incurred by her on the litigation should be allowed as a deduction.

The Income-tax Officer held that the allowance received by her was not "agricultural income" in her hands and was not exempt under section 4 (3) (viii); he admitted the principle of the other claim but as the petitioner had not proved the actual amount expended by her on the litigation he fixed the expenditure incurred by her at Rs. 12,000.

Deducting this sum of Rs. 12,000 from the amount received by the petitioner as allowances, viz., Rs. 83,254, the Income-tax Officer assessed the petitioner to income-tax and super-tax on the balance of Rs. 71,254. A copy of the order of the Income-tax Officer is appended as Annexure D.*

6. Against this assessment the petitioner unsuccessfully appealed to the Assistant Commissioner. A copy of the Assistant Commissioner's order is appended as Annexure E.*

The petitioner now requires me to refer for the opinion of the High Court the following question of law:—Whether on a construction of the wills by the late Sri Raja Varada Appa Rao Bahadur Garu the amount paid to the appellant out of the income of the estate is not agricultural income under the Act.

To claim exemption from payment of tax on the ground of "agricultural income" under section 4 (3) (viii) read with section 2 (1) of the Income-tax Act, an assessee should prove either: (1) that the income was rent or revenue derived by him from land which is used for agricultural purposes and is assessed to land revenue in British India, or is subject to a local rate assessed and collected by officers of Government as such, or (2) that it was income derived by him from such land by agriculture.

The income was in this case derived by the petitioner from the legacy bequeathed under her father's will. The will itself does not direct the executrix to pay the allowance to the petitioner from any specific land or lands used for agricultural purposes. It could have been paid out of the non-agricultural income of the estate just as much as out of the agricultural income and it was not contended or proved that the ultimate source from which the executrix found the money to pay the daughter was identifiable. Even if this had been the contention I do not consider that it affects the character of the income so far as the petitioner is concerned, for she derives it not from any land which she owns or possesses, but from the legacy bequeathed to her by the testator. I am therefore of opinion that the amount in question is not agricultural income within the meaning of the Income-tax Act.

V. Govindarajachari, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

The only question in this case is whether the legacy received by the assessee under the terms of her father's will and in respect of which she got a decree is exempt from the payment of income-tax, being agricultural income. Her father was the Zamindar of Gannavaram and he executed a will which is annexed as Exhibit C.* Under the will he appointed his wife as the executrix, gave her a life estate in the property and directed her to give his daughters a sum of Rs. 600 each per month. This sum of Rs. 600 was not paid and it fell into arrears. The daughters got a decree for Rs. 80,000 in the Sub-Court of Bazwada and this sum is taxed as income.

It is argued for the assessee that she got a rent charge on the income of the estate in respect of the amount that the executrix had to pay and that this sum of Rs. 600 should be treated as agricultural income as defined in section 2 (1). We think that this legacy cannot be brought under that clause and that she was rightly assessed on the amount she realised as arrears of maintenance. We answer the reference accordingly and direct that the assessee should pay Rs. 250 as costs of this reference.

(297) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Justice Sir C. V. Kumaraswami Sastriar, Kt., Mr. Justice Odgers and Mr. Justice Wallace.

(15th March, 1929).

Messrs. M. K. M. Mahammed Hassana Labbai & Co. . . . Assesseees.

v.

The Commissioner of Income-tax, Madras . . . Referring Officer.

Income-tax Act (XI of 1922), Secs. 24 & 26—Succession to business—Basis of assessment—One assessment on total income of predecessor and successor—Set off of loss of successor.

Where a firm is succeeded by another firm, the assessment must be on the footing that there is only one assessee whose total income assessable under Sec. 26 of the Income-tax Act will be the total income of the predecessor plus the total income or less the loss, as the case may be, of the successor during the same period.

Western India Turf Club, Ltd. v. Commissioner of Income-tax, Bombay, 2 I. T. C. 490 (P.C.), applied.

Case (O. P. No. 212 of 1928), stated under Sec. 66 (1) of Income-tax Act (XI of 1922), by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

CASE.

I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (1) of the Income-tax Act, XI of 1922.

* Not printed.

2. The petitioners Messrs. M. K. M. Mahammad Hassana Labbai & Co., are an unregistered firm carrying on business in hides at Ellore. The partners of the firm and their shares are as under:—

M. K. M. R. Mahammad Hassana Labbai and Company, Colombo.	.. 27/64 shares
M. K. M. K. Mahammed Hassana Labbai of Kayal- patnam.	.. 27/64 shares.
M. K. S. Mahammed Labbai of Kayalpatnam.	.. 10/64 shares.

The petitioners were also carrying on business in partnership with others at Madras and Cuttack.

3. They are assesseees on the file of the Income-tax Officer, Ellore. For the assessment of the year 1926-27 based on the profits of the official year 1st April 1925, to 31st March 1926, the Income-tax Officer, Ellore, called on them under section 22 (2) of the Income-tax Act to make a return of their income. The petitioners made a return showing a loss of Rs. 16,411 from their business at Ellore. They also represented to the Income-tax Officer that the firms carrying on business at Madras and Cuttack in which they were partners were assessed to tax separately by the Income-tax Officers of the respective areas. The Income-tax Officer accordingly excluded from the computation the share of profits and gains derived by the petitioners from those partnerships, confined himself to the examination of the accounts of their Ellore business and determined the loss sustained by the petitioners from that business at Rs. 8,170. He therefore declared them not liable to tax.

4. Subsequently to the assessment, the Income-tax Officer, Madras, reported to the Income-tax Officer, Ellore, that the business carried on at Madras by the petitioners in partnership with one M. K. K. T. Mahammed Ismail of Ellore was not assessed to income-tax at Madras, that the partnership carried on business from 16th February 1925 to 3rd November 1926 on which date the partner Mahammad Ismail retired from the business and that thereafter the petitioners became the proprietors of the business which they were carrying on. As the income derived by the petitioners from their Madras business had thus escaped assessment the Income-tax Officer, Ellore took action under section 34 to assess the profits and gains of that business. He issued a notice under section 22 (2) read with section 34 of the Income-tax Act and called on the petitioners as "successors" to the Madras business within the meaning of section 26 of the Income-tax Act to make a return of the income of that business. The petitioners failed to comply with the terms of that notice and the Income-tax Officer therefore assessed them under section 23 (4) on an income of Rs. 35,000 which he fixed to the best of his judgment to be the income of the Madras business.

5. The petitioners applied to the Income-tax Officer under section 27 of the Income-tax Act, but the latter declined to re-open the assessment as he was not satisfied that the petitioners were prevented by sufficient cause from making a return of their income. Against this order the petitioners appealed unsuccessfully to the Assistant Commissioner. A copy of the Assistant Commissioner's order marked Annexure A.* is enclosed and forms part of the case.

6. The petitioners now require me to state a case and refer for the decision of the High Court the following question of law:—"Where a person has succeeded to a business and is assessed on the profits thereof under section 26, should those profits be added to or set off against his other income or losses of the previous year for the purposes of determining his total income, or should they be treated as the subject of a separate and distinct assessment"?

* Not printed,

7. My opinion on the question is as follows:—During the year of account, viz., 1st April 1925 to 31st March 1926 the Madras business was carried on by a partnership consisting of Messrs. M. K. M. Mahammed Hassana Labbai & Co., and M. K. K. T. Mahammed Ismail of Ellore and that firm earned profits. Section 3 of the Income-tax Act, XI of 1922, enacts:—“Where any Act of Indian Legislature enacts that income-tax shall be charged for any year at any rate or rates applicable to the total income of an assessee, tax at the rate or those rates shall be charged for that year in accordance with and subject to the provisions of this Act in respect of all income, profits and gains of the previous year of every firm, etc.”. The income of the Madras firm had been determined to be Rs. 35,000 for the previous year, viz., 1st April 1925 to 31st March 1926, and had that firm been in existence in the year of assessment, viz., 1926-27, it would have been assessed under an Act of the Legislature, viz. The Indian Finance Act, 1927, on the income of Rs. 35,000 at the rate of 15 pies in the rupee. The business having been succeeded to at the time of the assessment by the petitioners the assessment for the year 1926-27, had to be made in the name of the “successors”, i.e., the petitioners under section 26 of the Income-tax Act which enacts:—“Where any change occurs in the constitution of a firm, or where any person has succeeded to any business, profession or vocation the assessment shall be made on the firm as constituted, or on the person engaged in the business, profession or vocation as the case may be at the time of the making of the assessment.”

The petitioners' case is that in assessing them on the profits and gains earned by their predecessors, the Madras firm, they should be deemed to have earned the profits and gains of such firm and permitted to set off against those profits any loss incurred by them during the same period; in other words, the total income of the successor for the purposes of an assessment under section 26 should be taken to be the total income of the predecessor plus the total income (or less the loss, as the case may be) of the successor during the same period. I am of opinion that this contention is untenable. I consider, reading sections 3 and 26 of the Income-tax Act, XI of 1922 that under the latter section the successor is merely liable to pay the tax that would have been payable on the profits made by the predecessor and that in computing the total income of the predecessor no account should be taken of the income or losses of the successor during the same period.

G. Ramakrishna Aiyar, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.*

The facts leading to this reference are shortly these:—M. K. M. Mahammed Hassana Labbai & Co., are a firm consisting of three partners carrying on business in hides at Ellore. On the 16th of February 1925 the firm started business in Madras in partnership with one Mahammed Ismail. This business went on from the 16th of February 1925 to the 30th of November 1926. From the Madras firm Mahammed Ismail retired and that business was continued by the remaining partners who were also partners in the Ellore business. The assessment year is 1926-27 and the accounting period is 1925-26. In the Ellore business there was a loss which according to the firm was Rs. 16,411; but the Income-tax Officer found it to be Rs. 8,170. It is stated that the loss in the Ellore firm was calculated after setting off the profits in the Madras firm. So far as the Madras firm was concerned, it was not taxed and in 1927 the Income-tax Officer acting under section

* Delivered by Kumarasamy Sastri, J.

34 read with sections 22 (2) and 26 issued two notices, one for 1926-27 and the other for the following year. We are now concerned with the notice for 1926-27. The claim of the assessee was that the loss at Ellore should be set off against the profits at Madras on the footing that there was only one firm and one assessee and consequently they were entitled to pay tax on the whole account being taken and after the set off. The question is whether we should treat the two firms as two different firms, or whether it should be taken that the firms should be assessed as if they are one firm and the profits and loss ascertained on that footing.

Section 26 enacts that "Where any change occurs in the constitution of a firm, or where any person has succeeded to any business, profession or vocation, the assessment shall be made on the firm as constituted, or on the person engaged in the business, profession or vocation as the case may be at the time of the making of the assessment." The question as to what should happen when there are two firms and one firm takes over the business of the other has been considered by the Privy Council in *Western India Turf Club, Ltd. v. Commissioner of Income-tax*(1). In that case the Western India Turf Club which was originally an unregistered association was converted into a limited company on the 1st of April 1925, the object of the company being to take over the assets, effects and liabilities of the Western India Turf Club. The question arose, at what rate the company should pay the super-tax from April 1925? The Act says that the super-tax has to be paid in respect of the total income for the previous year. But there was no total income for the previous year and the question was how it should be taxed. Their Lordships of the Privy Council pointed out that section 26 of the Act removes the difficulty. As a matter of fact, their Lordships said that for purposes of taxation the new company should be deemed to have been in existence in the previous year. With reference to the decision, *In the matter of Begg Sutherland and Co., Ltd.*(2), their Lordships of the Privy Council stated that if the question there decided should again arise that decision would require further consideration. In that case what was decided was that the old firm should be taken to have continued till the year of assessment although there was a new firm. That view their Lordships of the Privy Council were not disposed to endorse. The view taken by the Bombay High Court in *Western India Turf Club, Ltd. v. Commissioner of Income-tax, Bombay*(3), which was confirmed by their Lordships of the Privy Council(1) was that for purposes of taxation the new firm should be deemed to have been in existence in the previous year. To carry out this view there was an amendment of the Income-tax Act, (Act III of 1928).

Here, there is no dispute about the facts. The partners, after the retirement of Ismail, are the same in both the firms and there is no difference as regards shares; and it is conceded that there was practically an amalgamation. We think therefore that the tax ought to be levied on the footing that there is only one assessee and that under section 24 the loss of the Ellore firm should be set off against the profits of the Madras firm and the tax should be only on the balance. We answer the reference accordingly.

We direct that the Rs. 100 deposited by the firm should be refunded and we allow a fee of Rs. 150 on this reference.

(1) 2 I. T. C. 490.

(3) 2 I. T. C. 227.

(2) 2 I. T. C. 30.

(298) IN THE HIGH COURT OF JUDICATURE AT RANGOON.

Before Mr. Justice Heald and Mr. Justice Otter.

(18th March, 1929).

T. O. Foster

Assessee.

v.

The Commissioner of Income-tax, Burma.

Income-tax Act (XI of 1922), Secs. 13 & 66 (3)—Architect keeping accounts and assessed previously on earned income basis—Claim to be assessed on income received, if permissible.

The assessee, an architect, assessed in the past on the basis of his accounts wherein income earned every year and not income received was credited, claimed on an assessment for 1926-1927 to deduct a sum of Rs. 85,000 on the ground that the said sum though earned in the account year 1925-1926, was not actually received in that year. On an application under Sec. 66 (3) of the Income-tax Act to direct the Commissioner to state a case

HELD, that the assessment based on the accounting regularly employed by the assessee was in accordance with the provisions of Sec. 13 of the Act and that the assessee was not entitled to alter his system of accounting as claimed by him.

Application (Civil Misc. Application No. 141 of 1928), under Sec. 66 (3) of the Income-tax Act, (XI of 1922), for an order to direct the Commissioner of Income-tax, Burma, to state a case for the opinion of the High Court.

McDonnell, for the Assessee.

Foucar, for the Crown.

JUDGMENT.

The applicant, Mr. T. O. Foster, an Architect, made a return of his income for 1925-26, for the assessment of income-tax for the year 1926-27. The income-tax Officer after enquiry assessed his income at Rs. 1,64,316. Applicant appealed to the Assistant Commissioner of Income-tax who dismissed his appeal. He then applied to the Commissioner of Income-tax to state the case and to refer it to this Court under section 66 (2) of the Income-tax Act but the Commissioner refused.

Applicant now comes to us for an order requiring the Commissioner to state and refer the case under section 66 (3) of the Act.

The only question which is before us at present is whether or not a question of law arises on the Assistant Commissioner's order.

The sum in dispute is Rs. 85,000, which had been earned in 1925-26 but of which only Rs. 37,000 was actually received in 1926-27.

It is not denied that in the accounts of his business applicant gives credit for income earned and not income received during the year. This is of course to his advantage as otherwise so large an amount of income might be received in a particular year, although it had been earned in other years, that tax would have to be paid on it at a much higher rate than would be payable if it had been assessed in the years during which it was earned. It is not denied that in the past the

assessment has been made on the basis of income earned, and not of income actually received. In his return for 1926-27 applicant deducted this sum of Rs. 85,000 because although it was earned in the year 1925-26 on which the assessment was based it was not actually received during that year and only part of it was actually received during 1926-27. In effect therefore he claimed to be entitled to alter his system of accounting in respect of this item so as to exclude it from his assessment, although on the method of accounting adopted by him, it ought to have been included. He does not suggest that it is a bad debt, or that he will not receive it in due course. All that he says is that he did not actually receive it in the year on the income of which his assessment is based and that he received only part of it in the year for which he was being assessed. In our opinion the question whether or not he actually received it is immaterial. If he never receives it he will of course be entitled to an allowance in respect of it. What is material is that he keeps his accounts in such a way that credit ought to be given in them for this amount as income earned during the year on which the disputed assessment is based, and that under section 13 of the Income-tax Act income for the purpose of the assessment of income-tax is to be computed in accordance with the method of accounting regularly employed by the assessee.

It is clear that according to the method of accounting regularly employed by applicant, the amount in dispute ought to be included in the income of the year on which the disputed assessment is based and in these circumstances we fail to see that any question of law arises.

None of the questions of law mentioned in applicant's application arises. The first two do not arise because there is now no suggestion that the entry of Rs. 85,000 was a mistaken estimate of income actually earned, and the third does not arise because on the system of accounting adopted by applicant income earned and not income received is the basis of the assessment.

The application is dismissed with costs, advocate's fee to be five gold mohurs.

(299) IN THE HIGH COURT OF JUDICATURE AT RANGOON.

Before Justice Sir Benjamin Heald, Kt., and Mr. Justice Otter.

(25th March, 1929).

V. E. A. Chettyar Firm

Assessees.*

v.

The Commissioner of Income-tax, Burma.

Income-tax Act (XI of 1922), Secs. 33 & 66—Specific Relief Act (I of 1877), Sec. 45—Order passed in revision by Commissioner—Application for reference, if any—Jurisdiction under Sec. 45, Specific Relief Act.

In respect of an order passed by the Commissioner of Income-tax under Sec. 33 of the Income-tax Act, the Rangoon High Court has no jurisdiction either under Sec. 66 of the Act, or Sec. 45 of the Specific Relief Act to direct the Commissioner to state a case.

Application (Civil Misc. Application No. 96 of 1928), under Sec. 66 (3) of the Income-tax Act to direct the Commissioner of Income-tax, Burma, to state a case for the opinion of the High Court.

Foucar, for the Assessee.

JUDGMENT.

HEALD, J.:—The applicants, who are the V. E. A. Chettyar firm, made a return of their income for purposes of income-tax for 1927-28 and produced their books of account before the Income-tax Officer. That officer discovered certain omissions and other suspicious features in the accounts, and after enquiry held that applicants had not complied with the requirements of section 22 (4) of the Income-tax Act. He accordingly proceeded to make an assessment under section 23 (4) of the Act, that is, an assessment "to the best of his judgment", and assessed applicants on Rs. 1,50,000. No appeal lies against such an assessment, but applicants were entitled to apply for cancellation of the assessment under section 27 of the Act, and did so apply. The Income-tax Officer refused to cancel the assessment and applicants appealed to the Assistant Commissioner against the order refusing cancellation. The Assistant Commissioner set aside the assessment under section 23 (4) of the Act and directed that a fresh assessment be made in accordance with law. The Income-tax Officer then made a fresh assessment of Rs. 36,642 instead of Rs. 1,50,000. Applicants were satisfied with that assessment and took no further steps. The Commissioner however took up the case in review under section 33 of the Act and restored the assessment to Rs. 1,50,000. Applicants then applied to the Commissioner to state the case under section 66 (1), or section 66 (2) of the Act, but the Commissioner refused to do so.

Applicants now ask us for an order under section 66 (3) of the Act, or under section 45 of the Specific Relief Act, requiring the Commissioner to state the case and refer it to this Court.

It is clear that the case does not fall within the purview of section 66 (2) because the order on which the case arises is not an order under section 31 or 32 of the Act, but is the order of the Commissioner made under section 33 of the Act. There is therefore no question of our making an order under section 66 (3) of the Act, and the preliminary question which arises is whether we have power to make an order under section 45 of the Specific Relief Act.

For the application of that section it is necessary that the doing of the act ordered should be under any law for the time being in force, clearly incumbent on the person ordered to do the act, and it is therefore necessary to consider whether the stating of a case in circumstances such as those of the present case is clearly incumbent on the Commissioner of Income-tax.

Applicants rely on the judgment of their Lordships of the Privy Council in *Alcock's case* (1) and on a decision of a Full Bench of the High Court of Madras in *Abdul Kadir's case* (2).

In the Privy Council case the question arose under the provisions of section 51 of the Income-tax Act of 1918, which provided that if in the course of any assessment under the Act or any proceeding connected therewith, other than a proceeding under Chapter VII, a question has arisen with reference to the interpretation of any of the provisions of the Act or of any rule thereunder the Chief Revenue authority "may", either on its own motion or on reference from any

(1) 1 I. T. C. 22

(2) 2 I. T. C. 155

Revenue Officer subordinate to it, draw up a statement of the case and refer it with its own opinion thereon to the High Court, and "shall so refer" any such question on the application of the assessee, unless it is satisfied that the application is frivolous or that a reference is unnecessary. Their Lordships pointed out that under the latter part of that section if the assessee applies for a case the Authority must state it, unless he can say that it is frivolous or unnecessary, and that it will be a misfeasance and a breach of the statutory duty if he does not do it. As for the earlier part they said that although the word "may" does not mean "shall", nevertheless there may be circumstances which couple with the power a duty to exercise it, and they held that supposing there was a serious point of law to be considered there did lie a duty upon the Chief Revenue authority to state a case for the opinion of the Court and that if he did not appreciate that there was such a serious point it is in the power of the Court to control him and to order him to state a case. It is to be noted however that there was in section 51, no provision similar to that of the present section 66 (3) which gives the High Court express power to require the Commissioner of Income-tax to state a case and refer it and the intention of the Legislature in amending the Act was doubtless to state expressly the conditions for the exercise of the power of the Court to require the Commissioner to state and refer a case.

The Madras case was decided under the present Act and was similar to the present case in that an order under section 33 of the Act had been made by the Commissioner. In that case the learned Judges said that as to orders in review passed by the Commissioner under section 33 there is nothing to operate upon except section 66 (1) and the assessee has no remedy unless we hold that the Court has power to order the Commissioner to state a case embodying any point of law that may arise in the course of proceedings under section 33. They went on to say that unless the Court had such power the result would be that the Commissioner by calling up the records under section 33 would be in a position to **burke any further enquiry whatever, that they did not think that that could have** been intended, and that accordingly they held that the principle of *Alcock's* case must be applied to orders under section 33.

If that decision is correct, it settles the preliminary question which arises in the present case, but with all respect I suggest that it is not correct. Where the Legislature has in a special Act laid down particular conditions for the exercise of a power by the Court, I do not think that we are justified in disregarding those conditions and holding by reference to a general Act that we have powers beyond those given in the special Act. I entirely agree that the Act is defective and needs amendment, but I do not think that for that reason we are justified in going beyond its express terms and holding that we have powers which the Act itself does not confer.

I would therefore hold that in the circumstances of the present case we have no power under the Income-tax Act to require the Commissioner to state and refer the case, and that we are not entitled to have recourse to section 45 of the Specific Relief Act for that purpose.

I would accordingly dismiss the application, but in the circumstances I would make no order for costs.

OTTER, J. :—The short history of this case is that on the 24th June 1927 the applicant firm having been served with a notice under section 22 (2) of the Income-tax Act of 1922 returned an income of Rs. 16,826-8-0 from its business for the year 1927-1928. On 30th June 1927, notice under sections 22 (4) and 23 (2) of the Act was served on the firm, and in response the agent appeared and produced certain account books of the firm. Upon examination, the books

appeared to disclose large payments to two Chettyar Firms. Upon enquiry as to the names and addresses of the persons to whom these payments were made, and although adjournments were granted to enable the information to be obtained, the Income-tax Officer was informed by the agent that he could not furnish the names and addresses required. Furthermore the Income-tax Officer had received information that two advances had been made by the firm, viz., Rs. 5,000 on a mortgage deed and another of Rs. 3,000 upon a pro-note. No entry in the books regarding either of these transactions appears in the books produced. For these reasons the Income-tax Officer came to the conclusion that the applicant firm were keeping two sets of account books and that therefore they had not complied with the notice dated 30th June 1927 and he proceeded to assess the applicant firm under section 23 (4) of the Act at Rs. 1,50,000. On an application under section 27 of the Act the Income-tax Officer refused to cancel his assessment, and on appeal to the Assistant Commissioner the latter by an order of 10th March 1927, cancelled the assessment and ordered a fresh assessment to be made. Thereupon the Income-tax Officer reassessed the applicant firm at Rs. 36,642.

On the 12th June 1928, the Commissioner of Income-tax, Burma, called upon the applicant firm under section 33 of the Act to show cause why the order of 10th March 1927, should not be set aside and the original assessment restored. By an order dated 7th July 1928 the Commissioner of Income-tax, (after hearing the applicant firm) set aside the order of 10th March 1927 and restored the original assessment of Rs. 1,50,000.

The applicant firm applied to the Commissioner of Income-tax to state a case for the opinion of this Court under section 66 (2) or section 66 (1) of the Act. This the Commissioner refused to do, and this Court is now asked to direct the Commissioner under section 66 (3) of the Act, or under section 45 of the Specific Relief Act (read with section 66 (1) of the Income-tax Act) to state a case for the consideration of this Court.

The first question arising is whether, assuming a question of law arises, this Court has power to make the order asked for. It is now admitted that the application cannot be made under section 66 (2) of the Act, for this provision applies only to orders passed under sections 31 and 32 of the Act. It is said however that we can act under section 45 of the Specific Relief Act read with section 66 (1) of the Income-tax Act. It must be borne in mind that section 66 of the present Income-tax Act takes the place of section 51 of the Act of 1918, the latter section having been repealed by the present Act. Section 51 of the old Act was a general section which empowered the Chief Revenue Authority "in the course of any assessment, or any proceedings" (other than a proceeding under Chapter 7 of that Act) "to state a case upon a question with reference to the interpretation of any of the provisions of the Act and shall so refer any such question on the application of an assessee unless it is satisfied that it is frivolous or vexatious."

Section 66 of the present Act is different. By sub-section (1) it is provided that if in the course of *any assessment under the Act* a question of law arises, the Commissioner may either on his own motion or on reference from an Income-tax authority draw up a statement of the case and refer it to the High Court. Sub-section 2 provides that "within one month the assessee may require the Commissioner to refer any question of law arising out of such order to refer it to the High Court." Sub-section 3 gives an assessee the right upon refusal by the Commissioner under sub-section 2 to apply to the High Court, and this Court may require the Commissioner to state a case. Thus so far as section 66 as it stands alone is concerned an assessee can only get a case stated where an order was passed under section 31 or section 32 of the Act.

It is said however that by virtue of section 45 of the Specific Relief Act read with sub-section 1 of section 66 of the Income-tax Act, we have power to order the Commissioner to state a case in respect of an order under section 33 of the Act and a number of cases were cited before us.

Alcock, Ashdown and Company, Ltd. v. Chief Revenue Authority of Bombay (1), was a case decided by the Privy Council under the old section 51; and upon the wording of that section it was held to be the duty of the Revenue authority to state a case where a serious question of law arises, the reason being that though the sub-section was not mandatory upon the Revenue authority, there may be circumstances which would couple with the power given by the Statute a duty to exercise it.

Trikamji Jiwan Das v. The Commissioner of Income-tax, Bihar and Orissa (2), arose under the present Act. A Bench of the Patna High Court had directed the Commissioner to state a case under section 66 (1) of the Act *on the application of an assessee*. The matter came before the Chief Justice and another Judge of that Court, and the Chief Justice in his Judgment expressed grave doubt whether the Commissioner could have been so directed and pointed out that in the Bombay case of *Alcock, Ashdown and Company, Ltd.* (1), it was necessary to invoke section 45 of the Specific Relief Act. But as the matter was before the Court it was dealt with and the assessee's application dismissed upon the facts. I would observe that neither of these cases is an authority for the proposition argued before us. The first was decided under the old section 51, and the remark by the Chief Justice in the second was *obiter*. *In re Sheik Abdul Kadir Marakayar & Co.* (3), was also cited. There (in a case arising under section 33) and relying on the case of *Alcock, Ashdown and Company, Ltd.*, a full Bench of the Madras High Court held that it could not have been intended by the Legislature to allow a Commissioner who takes action under section 33 to escape any further enquiry. It was not argued, so far as the report discloses, that as the wording of section 66 (1) makes no mention of an assessee the *Alcock Ashdown* case should be distinguished. An *obiter dictum* of the Calcutta High Court was relied on to the effect that in such a case, and upon a properly constituted application, under section 45 of the Specific Relief Act, the High Court might possibly pass an order such as is asked for in the present case; see *Kumar Sarat Kumar Roy v. The Commissioner of Income-tax, Bengal* (4). Two other cases were cited where applications under section 66 (1) of the Act were refused. In neither of these was section 45 of the Specific Relief Act relied on; see *Sin Seng Hin v. Commissioner of Income-tax, Burma* (5), and *Ratanchand Khimchand Motishaw v. The Commissioner of Income-tax, Bombay* (6). In considering whether section 45 of the Specific Relief Act can assist the applicant it is necessary to consider the provisions of that section. Sub-section (b) of that section is as follows:—"that such doing or forbearing is, under any law for the time being in force, clearly incumbent on such person or Court in his or its public character, or on such corporation in its corporate character".

Under section 51 of the old Act (as the Privy Council held) it was incumbent upon the Revenue Authority *in a proper case* to state a case for the opinion of the High Court upon *the application of an assessee*. But, as the late Chief Justice of this Court said in *Sin Seng Hin's case* (5), "there is no provision permitting an assessee to move the High Court in respect of an order under section 33 of the present Act."

(1) 1 I. T. C. 221.

(2) 1 I. T. C. 406.

(3) 2 I. T. C. 155.

(4) 2 I. T. C. 279.

(5) 2 I. T. C. 39.

(6) 2 I. T. C. 225.

It is perfectly true that the case of *Sheik Abdul Kadir Marakayar & Co.*, is in favour of applicant's contention, and moreover that, as that Court thought, cases of apparent hardship might arise.

The learned Judges of the Madras High Court seem to have been under the impression that somewhere or other there is now a provision giving an assessee the right to ask for a case other than under section 66 (2) of the Act. The learned Chief Justice (at page 156) says, "that Court is asked to draw the inference that the power of the High Court was meant to be confined to cases under those sections (i.e., sections 31-32), and was by implication taken away in the case of orders under section 33." He does not go on to say however by virtue of what law, the right of an assessee to get such a case stated, exists.

This is not one of those cases where a statute has enacted something for a particular case only, that was already and more widely the law. In such cases it would be useless to argue that an intention to alter the general law is to be inferred from the partial or limited enactment. Here section 51 of the old Act which contained the whole law on the subject was repealed; and *after* the decision in *Alcock, Ashdown and Company, Ltd.*, by the Judicial Committee the legislature enacts in plain terms what the law is. There is now no other law. The position would be different if an assessee were mentioned in sub-section 1 of section 66. Then it might be said that "some law would be in force" within the meaning of section 45 (b) of the Specific Relief Act and the applicant might pray in aid that enactment to obtain a case.

For these reasons I think that in the present case this Court has no jurisdiction to entertain the application. It is unnecessary therefore to consider the merits of the application which must be dismissed, but without costs.

(300) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

*Before Justice Sir C. V. Kumaraswami Sastriar, Kt., Mr. Justice Odgers and
Mr. Justice Wallace.*

(26th March, 1929).

V. R. S. A. R. Arunachalam Chettiar

v.

... Assessee.*

The Commissioner of Income-tax, Madras. Referring Officer.

Income-tax Act (XI of 1922), Secs. 4 (2) & 26—Hindu joint family—Allotment of foreign family business to co-parcener on partition—Assessment as successor to business—Sec. 26, if applies to foreign business—Remittances prior to partition—Successor, if assessable—Profits earned before partition—If capital assets on partition.

The assessee, a member of a Hindu joint family which owned a share in a foreign money-lending business at Taiping, got inter alia the family interest in the foreign business as his share in the partition effected on 5th November 1925. Prior to partition there was a remittance from Taiping of Rs. 29,218 and subsequent thereto a further remittance of Rs. 15,037. On an assessment of these

* 57 M.L.J. 300 ; 30 L. W. 541 ; 1929 Mad, 769,

sums under Secs. 4 (2) and 26 of the Income-tax Act, the assessee contended that they were his capital assets, that he was not assessable in respect of the sums received by the joint family and that the provisions of Secs. 26 would not apply.

HELD, (1) that the sum received after partition was assessable under Sec. 26 of the Act, the assessee being the successor of the business allotted to him under the partition,

(2) that having regard to the provisions of Secs. 14 and 16 of the Act, the assessee was not taxable in respect of the sum received by the joint family before partition, the joint family alone being chargeable therefor.

The provisions of Sec. 26 of the Act are not limited to businesses in British India.

Where on a partition of Hindu joint family a business allotted to a member as a going concern was continued as before without closing the accounts at the date of the partition, the business profit earned before partition would not lose the character of profits and become merged in his capital assets.

Case (O. P. Nos. 127 and 217 of 1928), stated under Secs. 66 (2) and (3) of the Indian Income-tax Act, (XI of 1922) by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

CASE. [O. P. 127 of 1928.]

I have the honour to refer the following case for the opinion of the Hon'ble the Judges of the High Court under section 66 (2) of the Indian Income-tax Act, 1922.

2. The applicant, Arunachalam Chettiar is a Nattukottai Chetti, residing at Kilasevalpatti in the Ramnad district within the jurisdiction of the Income-tax Officer, Second Circle, Karaikudi.

3. Till November 1925, he was a member of an undivided Hindu family which was carrying on money lending business at Rangoon and Myingyan in Burma, Penang in the Straits Settlements and Taiping and Sungipattani in the Federated Malay States. The business at Taiping was a partnership of four persons in which the family had a 50/76ths share. On 5th November 1925 the family became divided and at the partition the family's interest in the business at Taiping was allotted to the share of the applicant.

4. The applicant carried on the business at Taiping with the other partners throughout the year 1925-26. In August 1926 one of the other partners ceased his connection but the business was continued by the applicant with the other partners.

5. During the year 1925-26 remittances were made from Taiping to British India to the extent of Rs. 44,255, out of which Rs. 29,218 was sent prior to the date of partition and Rs. 15,037 subsequently. It is admitted that the profits of the business were more than the remittances.

6. In 1926-27 the Income-tax Officer proposed to treat the entire amount remitted as profits received in British India during the year of account 1925-26. The applicant objected that the remittances made to the family must be treated as capital allotted to him at the partition and could not be treated as his income. The Income-tax Officer held that the applicant had succeeded to the business of the family at Taiping and was therefore under sections 4 (2) and 26 of the Income-

tax Act liable to pay tax on the profits remitted to the family. He accordingly assessed him on an income of Rs. 45,931 made up as under and levied tax amounting to Rs. 4,306-1-0.

Property

.. Rs. 100

Business:—

Headquarters money lending .. Rs. 1,576

Remittances from Taiping .. Rs. 44,255

Rs. 45,831

Rs. 45,931

7. The applicant appealed to the Assistant Commissioner who while upholding the Income-tax Officer's view that the remittances made to the family were taxable in the hands of the applicant, considered that, in accordance with the decision of the Allahabad High Court in the case of Messrs. Begg Sutherland & Company Limited(1), the profits of the family business to which he succeeded should be computed and taxed separately. He accordingly reduced the tax payable by the applicant to Rs. 2,609-9-0 as under:—

	Rs. s. p.
Tax at one anna in the rupee on Rs. 29,218 remitted to the family ..	1,826-2-0
Tax at 9 pies in the rupee on the other income of the applicant Rs.16,713 (including Rs. 15,037 from remittances) ..	783-7-0
	<u>2,609-9-0</u>

8. The applicant requires me under section 66 (2) of the Income-tax Act to refer certain questions of law for the decision of the High Court. I refer the following questions with my opinions thereon.

9. *Question 1.* "Whether in the circumstances stated above, section 26 of Act XI of 1922 will govern this case in respect of the partnership at Taiping which is situated outside British India." I find nothing in section 26 to warrant the view that it only applies to a business carried on in British India. In my opinion it applies whether the business succeeded to is situated in British India or outside it.

10. *Question 2.* "Whether there can be any succession to a part of the same business." The doctrine that there cannot be a succession to part of a business does not apply to the facts of this case. The family had a business at Taiping distinct from its other businesses; separate accounts were maintained for that business and its profits could be separately ascertained. The fact that the family was carrying on that business in partnership with others makes no difference. The applicant succeeded to the whole of the family's interest in the business which after the succession was carried on as before.

11. *Question 3.* "Whether the petitioner can be made liable under section 4 (2) in respect of the profits, if any, received from Taiping by the extinct joint family." Under section 4 (2) of the Income-tax Act profits of a foreign

business received or brought into British India within three years of the end of the year in which they accrued or arose are deemed to have accrued in British India in the year in which they are so received or brought. The profits of the Taiping business in the present case would therefore have been taxed in the hands of the joint family if it had existed at the time of the assessment. They have been taxed in the hands of the applicant who succeeded to the business of the joint family, by virtue of the special provisions of section 26. I am of opinion that the assessment was rightly made.

12. *Question 4.* "Whether the action of the Assistant Commissioner in having varied the order of the Income-tax Officer by making two assessments on the petitioner, one on the petitioner himself individually and the other as a successor to the joint family is legal with reference to section 31 of the Act, as such an action can only be taken by starting fresh proceedings under section 22 of the Act." The applicant as successor to the business at Taiping was under section 26 liable to pay tax on the profits remitted to the joint family. He was also liable to pay tax on the profits remitted after partition along with his other income. The Income-tax Officer, combined the incomes of the family and the applicant and computed the tax on the aggregate income. The Assistant Commissioner varied the assessment by computing the tax separately on the two incomes and in the result reduced the demand from Rs. 4,306-1-0 to Rs. 2,609-9-0. He had all the materials for making this revision and section 31 (3) (a) authorised him to reduce the assessment. There was no necessity in this case for starting fresh proceedings under section 22 (2) and in my opinion there was no irregularity in the procedure adopted by the Assistant Commissioner.

CASE. [O P. 217 of 1928.]

I have the honour to refer the following case for the opinion of the Hon'ble the Judges of the High Court under section 66 (3) of the Indian Income-tax Act, 1922.

2. The petitioner Arunachalam Chettiar is a Nattukottai Chetti residing at Kilasevalpatti in the Ramnad District within the jurisdiction of the Income-tax Officer, Second Circle, Karaikudi.

3. Till November 1925 he was a member of an undivided Hindu family carrying on money lending business at Rangoon and Myingyan in Burma, Penang in the Straits Settlements and Taiping and Sungaipattani in the Federated Malay States. The business at Taiping was a partnership of four persons in which the family had a 50/76ths share. On 5th November 1925, the family became divided and at the partition the family's interest in the business at Taiping was allotted to the share of the petitioner.

4. The petitioner carried on the business at Taiping with the other partners throughout the year 1925-26. In August 1926 one of the other partners ceased his connection but the business was continued by the applicant with the other partners.

5. During the year 1925-26 remittances were made from Taiping to British India to the extent of Rs. 44,255 out of which Rs. 29,218 was sent prior to the date of partition and received by the joint family and Rs. 15,037 was remitted subsequent to the partition to the petitioner. It is admitted that the profits of the business were more than the remittances, and that such profits accrued or arose to the joint family prior to the partition.

6. In 1926-27 the Income-tax Officer proposed to treat the entire amount remitted as profits received in British India during the year of account 1925-26. The petitioner objected that the remittances must be treated as capital allotted to him at the partition and could not be treated as his income. The Income-tax Officer held that the petitioner had succeeded to the business of the family at Taiping and was therefore under sections 4 (2) and 26 of the Income-tax Act liable to pay tax on the profits of the family remitted to British India. He accordingly assessed him on an income of Rs. 45,931 made up as under and levied tax amounting to Rs. 4,306-1-0.

Property .. Rs. 100

Business:—

Headquarters money lending .. Rs. 1,576
Remittances from Taiping .. Rs. 44,255

Rs. 45,831

Rs. 45,931

7. The petitioner appealed to the Assistant Commissioner who while upholding the Income-tax Officer's view that the remittances made to the family were taxable in the hands of the applicant, considered that, in accordance with the decision of the Allahabad High Court in the case of Messrs. Begg Sutherland & Company Limited(1), the profits of the Taiping business to which he succeeded should be computed and taxed separately. He accordingly reduced the tax payable by the applicant to Rs. 2,609-9-0 as under.

	Rs. a. p.
'Tax at one anna in the rupee on Rs. 29,218 remitted to the family'	.. 1,826-2-0
'Tax at 9 pies in the rupee on the other income of the petitioner, viz., Rs. 16,713 (which includes Rs. 15,037 referred to in paragraph 5.)'	.. 783-7-0
	<u>2,609-9-0</u>

8. The petitioner required me under section 66 (2) of the Act to refer certain questions of law for the decision of the High Court. In my letter No. 534/27, dated 24th August 1927, I referred four questions and by an order of the same date, I refused to refer the other questions. One of those was "whether what was got by an individual for his share in the partition amongst the family members is not capital to him and whether the sums divided among the family members in the course of partition will retain the character of profits, if any, even after the sums came into the hands of the divided members."

9. The petitioner subsequently moved the High Court under section 66 (3) of the Income-tax Act and contended that the correctness of the assessment made on him individually on a remittance of Rs. 15,037 received by him subsequent to the partition depended on a determination of the question referred to in paragraph 8 above. In the order quoted above I have been directed to state a case and refer the following question. "Whether in a partition effected between the members of a Hindu joint family, the properties and assets allotted to each

co-parcener would not be capital assets in his hands and whether any sums of money received by the separated co-parcener from a business out of British India allotted to him under the partition would be assessable as a remittance of the profits of the business earned prior to partition."

Before I proceed to give my opinion on the question that I have been directed to refer I respectfully invite the attention of their Lordships to this preliminary question "Whether the petitioner is entitled to move the High Court for a direction to the Commissioner to refer a question of law which was not raised before him in the course of proceedings under section 66 (2) of the Income-tax Act." In *P. Thiruvengada Mudaliar v. Commissioner of Income-tax, Madras* (1), a Full Bench of this Court has held that an assessee cannot be allowed to argue before the Court a question of law which was not raised before the Commissioner in application under section 66 (2). In the present case it will be seen that the question which the petitioner seeks to raise before the High Court is not the same as the one which he required me in his application under section 66 (2) to refer to the High Court except perhaps, in regard to the first branch of the question now raised. This branch of the question, though phrased a little differently, seems to be in substance the same as the question raised before me, but except to this extent I venture to submit that the question now raised should not be made the subject matter of decision in this case.

I now proceed to give my opinion on the question that I have been directed to refer.

The petitioner's contention is:—(1) that the share in the business at Taiping which was allotted to him at partition was one of the assets of the family and therefore capital, (2) that the accumulated profits at Taiping which came under his control as a result of the partition must be regarded as a portion of this asset; and therefore (3) that any subsequent drawing upon those profits constitutes a withdrawal of his capital.

The first part of this argument need not be disputed. The second part implies that the petitioner received the accumulated profits at partition. In my opinion this is not an accurate statement. What he received at partition was the right to draw upon those profits. The profits did not, I think, lose their character as such merely because the right to draw upon them was transferred to the petitioner. Their character as "profits and gains of a business accruing or arising without British India to a person resident in British India" to use the language of section 4, sub-section 2, was not affected by the partition. The conclusion that in drawing upon the profits accumulated by the family the petitioner was really withdrawing part of the capital of the foreign business is therefore, in my opinion, incorrect.

The above is my opinion on the first part of the question. The second part of the question as has been observed already, is new. If it is meant to be a mere expansion of the first, that part is answered above. If it is intended to raise new points those points were not raised before me when I refused to make the reference and I therefore find myself unable to express an opinion on them.

K. S. Krishnaswami Ayyangar and P. R. Srinivasan, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

The assessee prior to the 5th of November 1925, was a member of a joint undivided family consisting of his father and brothers. The joint family so constituted was entitled to 50/76ths share in a money lending business carried on at Taiping in the Federated Malay States. On the 5th of November there was a partition amongst the members of the joint family and in that partition the interest of the family in the Taiping business as a going concern fell to the share of the assessee. Prior to the date of the partition there had been a remittance to the joint family of Rs. 29,218 in the year Krodhana (13th April 1925 to 12th April 1926). Subsequent to the partition there was a further remittance of Rs. 15,037. These sums were remitted not in one lump sum but that makes no difference. The year of account in the present case is Krodhana (13th April 1925 to 12th April 1926), and the year of assessment 1926-27. The accounts were kept on cash basis. The Income-tax Officer over-ruled the objections of the assessee and assessed the assessee on these sums as being foreign profits brought into British India and taxable under section 4 (2). Hence this reference.

The contention for the assessee is that, as he got the Taiping business for his share of the joint family, what he got was capital and that he could not be taxed as having received any profits. It is also contended that as the moneys were received by him as a member of the joint family, he could not be taxed, and it is the joint family that should be taxed and not the assessee individually, that under section 14 of the Income-tax Act he is not liable to assessment, that the fact that the joint family ceased to exist during the year of assessment does not make any difference so far as he is concerned, that there was no provision in the Act for taxing a joint family dissolved during the year of assessment or account, and that this defect has only been removed by sections 25-A and 26 inserted by an amendment of the Act (III of 1928). It is also contended that section 26 can have no application as the firm is situate outside British India and it is only the income that is brought into British India that is taxable.

There is no dispute about the facts as set out. Section 4 (2) enacts that "profits and gains of a business accruing or arising without British India to a person resident in British India shall, if they are received in or brought into British India, be deemed to have accrued or arisen in British India and to be profits and gains of the year in which they are so received or brought, notwithstanding the fact that they did not so accrue or arise in that year, provided that they are so received or brought in within three years of the end of the year in which they accrued or arose."

It is therefore clear that had the joint family of which the assessee was a member continued without partition during the year of assessment, the joint family would have been taxable in respect of the sums of Rs. 29,218 and Rs. 15,037 received in British India, as it is not disputed that the members of the joint family were residents in British India and that the sums remitted were profits.

Section 26 as it stood in 1925-26 ran as follows:—"Where any change occurs in the constitution of a firm or where any person has succeeded to any business, profession or vocation, the assessment shall be made on the firm as constituted or on the person engaged in the business, profession or vocation, as the case may be, at the time of the making of the assessment." I do not think that the contention that section 26 has application only to firms in British India and has no application to firms outside British India can be accepted.

Section 4 (1) makes the profits of a company outside British India taxable if brought into British India. There is nothing in section 26 which limits the scope of the section to firms in British India. Section 4 declares that the income of a foreign firm is taxable. In dealing with the income which is so taxable and determining who is the person to pay the tax, there is no reason why the provisions of section 26 should not be applicable. Section 26 only deals with the persons who are to be assessed. Where there is a change I am of opinion that section 4 enacts when the profits of a foreign firm are taxable and section 26 states whom you have to reach to collect the tax. The mere fact that the firm if it brought no profits into British India would not be taxable does not affect the question. Any enquiry for the purpose of ascertaining whether the sum is taxable or not, and whether it is profits or capital got back and, who is to pay the tax is within the scope and jurisdiction of the Income-tax Officers, and for that purpose the accounts of the foreign firm may be scrutinised. It is not therefore correct to say that in the case of foreign firms whose profits are brought into British India and taxable under section 4 (2), the other provisions of the Income-tax Act are inapplicable.

The next question is whether in the case of partition of an undivided family the members of which are carrying on business, section 26 applies, where during the year in question the business falls to the share of one or more of the members. Having regard to the wording of section 26, I do not see anything to prevent its application. Prior to the partition, all the members of the joint family constituted the firm. By reason of the partition certain members who constituted the firm ceased to have any interest in the firm and their interest by reason of the partition devolved on the person or persons to whom their shares in the business have been allotted. It is difficult to distinguish this case from the case of an ordinary partnership where, there are, say, four partners and three of them retire from the business assigning their interest to the fourth partner and the fourth partner continues the business. I am of opinion that in cases where there has been a partition of an undivided Hindu trading family, section 26 applies and the person who becomes entitled to the business during the year in question cannot escape liability unless he can bring himself within any other section exempting him from liability.

The next question is whether in the case of a partition amongst the members of a joint family where a person becomes entitled on partition to a foreign business as his share, the profits earned in the year in which the partition takes place lose the character of profits as having merged in the capital and should be treated as the capital of the person who gets the business on partition. The argument of Mr. Krishnaswami Ayyangar for the assessee is that where a partition takes place between the members of an undivided family, a person in consideration of his share in all the joint family properties gets a particular item which presumably is equivalent to his share in the properties which were clubbed together for ascertaining his share and therefore it should be taken that what he gets is not profits or capital in the business but the value of the whole of the business as representing his share and so far as he is concerned it is his capital.

It is argued that the position is similar to that where a limited company is wound up and the assets distributed, where there is no question of taxable profits as regards the share-holders to whom the assets are distributed. Reference has been made to *Inland Revenue Commissioners v. Burrell*(1), where it was held that on the winding up of a limited Company, the undivided profits of past years

(1) 9 Tax Cas. 27 ; 1924 2 K. B. 52.

and of the year in which the winding up occurred, were assets and not profits for the purpose of taxation, and to *Inland Revenue Commissioners v. Blott*; *Inland Revenue Commissioners v. Greenwood* (1), where it was held that where a limited company passed a resolution that out of its undivided profits a bonus should be paid to the shareholders and that such payment should take the form of certain shares being allotted to them, the shares so allotted could not be treated as part of the total income for the purpose of super-tax.

I do not think the principle of these cases has any application to cases where on a partition between the members of a joint family a business as a going concern is allotted to the share of one member. It is not suggested in the present case, that when the business was allotted, the accounts of the business were closed, profits ascertained and such ascertained profits added to the capital and a new business in which this capital was invested was carried on. Nor is it suggested that the business was wound up. The profits remained as profits, the business went on as before and the only change was that instead of all the members of the joint family being interested in the business, one of them acquired the interests of the others and became the sole proprietor. So far therefore as the sum of Rs. 15,037 received by the assessee after the partition is concerned, I am of opinion that it is taxable.

As regards the sum of Rs. 29,218 received before the partition, it is not disputed that this sum was received by the joint family of which the petitioner was a member, and it seems to me that having regard to the provisions of sections 14 and 16 the assessee is not taxable. In a case like the present we should read sections 4 (2), 14, 16 and 26 together. No doubt section 26 says that, when there is a change, the person liable is the person engaged in the business at the time of making the assessment. But the section does not prevent him from claiming any of the exemptions conferred by the other sections of the Act.

Section 14 (1) runs as follows:—"The tax shall not be payable by an assessee in respect of any sum which he receives as a member of a Hindu undivided family. (2) The tax shall not be payable by an assessee in respect of— (a) any sum which he receives by way of dividend as a share-holder in a company where the profits or gains of the company have been assessed to income-tax; or (b) such an amount of the profits or gains of any firm which have been assessed to income-tax as is proportionate to his share in the firm." It will be noted here that, while sub-clause 2 only exempts cases where a company or a firm has already been assessed, sub-clause 1 puts no such limitation but states generally that the tax shall not be payable by an assessee in respect of any sum which he receives as a member of an undivided Hindu family.

Provision is made in section 3 for the taxation of undivided Hindu families, and it says that income-tax can be charged on the income, profits and gains of the previous year of every individual, company, firm and Hindu undivided family. Section 16 (1) runs as follows:—"In computing the total income of an assessee, sums exempted under the proviso to sub-section (1) of section 7, the proviso to section 8, sub-section (2) of section 14 and section 15, shall be included." Here again it will be noted that section 14 (1) is not to be included, i.e., any sum received by a member of an undivided Hindu family.

There was no provision in the Act until the recent amendment by which undivided families which became divided during the course of the year could be reached. To remedy this defect the legislature amended the Act by enacting

(1) 8 Tax Cas. 101; (1921) 2 A. C. 171.

section 25-A and by recasting section 26 of the old Act. Clause 1 of section 25-A provides for an enquiry by the Income-tax Officer when a partition is alleged, and an order by him as to whether he finds the partition proved. Clause 2 runs as follows:—"When such an order has been passed the Income-tax Officer shall make an assessment of the total income received by or on behalf of the joint family as such as if no separation or partition had taken place and each member or group of members shall in addition to any income-tax for which he or it may be separately liable and notwithstanding anything contained in sub-section 1 of section 14, shall be liable for a share of the tax on the income so assessed according to the portion of the joint family property allotted to him or it, * * * Provided that all the separated members and groups of members shall be liable jointly and severally for the tax assessed on the total income received by or on behalf of the joint family as such". In my view the provisions of sections 14 and 16 being clear and the amendment introduced by Act III of 1928 being much later than the period for which the income has been assessed, no consideration as to the inconvenience or as to any person escaping from taxation can arise. There is no ambiguity in the sections and the clear meaning of section 14 (1) is that where a member of an undivided Hindu family during the period when the family is joint receives any portion of the income of the joint family, he is not liable to taxation but it is the joint family which under section 3 should be charged. This is not a case where we have to construe a doubtful section.

In *Partington v. Attorney-General* (1), Lord Cairns observed as follows:—"I am not at all sure that, in a case of this kind—a fiscal case—form is not amply sufficient; because, as I understand the principle of all fiscal legislation, it is this: if the person sought to be taxed comes within the letter of the law he must be taxed, however great the hardship may appear to the judicial mind to be. On the other hand, if the Crown seeking to recover the tax, cannot bring the subject within the letter of the law, the subject is free, however apparently within the spirit of the law the case might otherwise appear to be. In other words, if there be admissible, in any statute, what is called an equitable construction, certainly such a construction is not admissible in a taxing statute, where you can simply adhere to the words of the statute." As observed by Lord Halsbury in *Lord Advocate v. Fleming* (2), in construing such Acts "we have no governing principle of the Act to look at; we have simply to go on the Act itself, to see whether the duty claimed is that which the legislature has enacted."

Reference has been made by Mr. Patanjali Sastri to section 5 (1) (f) of the Act of 1886 and section 12 (1) of the Act of 1918 and it is argued that all that was done by section 14 (1) of the present Act was to prevent double taxation and that if the undivided family ceased to exist, there is no reason for the individual member who receives the sum not being taxed.

In the present case I fail to see any reason why one member of an undivided Hindu family should be taxed for a sum received by all the members of the undivided family. The new amendment which I have referred to shows that the legislature intended that the member should only pay a tax proportionate to his share. There is no question of any equitable consideration in cases where one member of an undivided family after partition is sought to be made liable to pay tax on the whole sum which he and the other members of the family received before partition irrespective of his share. However this may be, it seems to me having regard to the decisions I have referred to we cannot in a fiscal enactment where the language is clear get beyond the plain meaning of the section. It is

(1) (1869) L. R. 4 H. L. 100.

(2) (1897) A. C. 145.

very probable that in the Income-tax Act of 1922 the legislature by oversight or owing to bad draftsmanship omitted to prescribe for cases where there has been a partition in an undivided family, but it has now been remedied by Act III of 1928. I do not think I can by any rule of construction practically make section 25-A retrospective by enacting that the same principle is to be applied to cases coming under the Act of 1922.

I am of opinion that the assessee is not taxable as regards the sum of Rs. 29,218 received before the partition by the joint family. Rs. 100 paid in O. P. 127 of 1928 will be refunded by the Commissioner.

ODGERS, J.:—I agree.

WALLACE, J.:—I agree.

301, IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Mr. Justice L. G. Mukerji and Mr. Justice Niamat Ullah.

(5th April, 1929).

Messrs. Kajorimal Kalyanmal

.. Assessee.

v.

The Commissioner of Income-tax, United Provinces .. Referring Officer.

Income-tax Act (XI of 1922), Secs. 22, 27 & 66—Notice for return giving 29 days—Legality—Sufficiency of cause for non-submission of return, if a question of law—Jurisdiction of High Court to determine points not raised before.

A notice under Sec. 22 (2) of the Income-tax Act giving the assessee 29 days time for filing the return is entirely illegal and this crucial defect cannot be cured by subsequent extensions of time.

The question whether the assessee was prevented by sufficient cause from submitting the return under Sec. 22 (2) is a mixed question of law and fact, the question of law being whether the facts alleged by the assessee, if accepted as true, may be treated as sufficient cause in law within the meaning of Sec. 27 of the Act.

It is open to the High Court under Sec. 66 to formulate questions of law that really arise in the case, though never raised before and answer them for the benefit of the Commissioner or the assessee.

Case (Misc. Case No. 6 of 1929), stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, United Provinces, for the opinion of the High Court.

CASE.

The assesseees who are members of an undivided Hindu family were served with a notice on April 13, 1928, under section 22 (2) of the Income-tax Act (XI of 1922), requiring them to submit on or before May 12, 1928, a return of their total income in the previous year. No return of income was submitted. On May 19, 1928, the Income-tax Officer then issued a notice under section 22 (4)

requiring the assessee to submit on May 28, 1928, their accounts for the two years ending *Dewali Samvat* 1983 and 1984. On May 28, 1928, Lala Kalyanmal the head of the family attended the Income-tax Office with the accounts which were seen by the Income-tax Officer. On being questioned as regards his return of income, Lala Kalyanmal said that he was unable to submit it as his books were not ready. The Income-tax Officer, therefore, examined the books in the condition in which they were and found, as a matter of fact, that they were almost complete so that the assessee could easily have submitted his return of income in a few minutes if he had chosen to do so. He drew the attention of the assessee to this fact and asked him to submit his return of income on that very day. The assessee did not, however, agree to this suggestion and insisted on being allowed time to complete his books before submitting his return. The Income-tax Officer, therefore, postponed assessment for five days, in other words, gave to the assessee five days more to avail himself of the opportunity provided in section 22 (3) of the Income-tax Act, which, for the present purpose, runs:—
 “If any person has not furnished a return under sub-section (2), he may furnish a return at any time before the assessment is made and any return so made shall be deemed to be a return made in due time under this section.”

In postponing the assessment proceedings for five days the Income-tax Officer informed the assessee that he would not defer them again and warned him at the same time that failure on his part would result in an assessment under section 23 (4). Precisely on the date to which the case was postponed, that is June 2, 1928, the assessee Lala Kalyanmal sent a petition accompanied by two medical certificates, briefly to the effect that his son Lala Har Narain could not complete the books owing to the illness of his wife whom he had to remove from Cawnpore on medical advice, and that he himself could not complete them because he was laid up with toothache. He, therefore, asked for further time until the return of his son. The Income-tax Officer naturally construed this request as an expression of the assessee's reluctance to avail himself of the facilities allowed by section 22 (3) of the Income-tax Act to submit a return of income at any time before an assessment had been made, even after the expiry of the time given in the original notice under section 22 (2). He, therefore, proceeded to make and did make an assessment to the best of his judgment on the same day, utilizing the information he had extracted from the books which the assessee had produced on May 28, 1928, and at the same time such other information as he had obtained from the accounts of local firms and as a result of his inquiries.

2. On July 2, 1928, after receiving the notice of demand which was served on June 2, 1928, the assessee made a petition to the Income-tax Officer under section 27 for reopening the assessment. After hearing the assessee, the Income-tax Officer rejected this petition and the Assistant Commissioner of Income-tax on appeal upheld his decision for reasons given in his appellate order.

3. The assessee now desires that I should make a reference to the Honourable High Court on the following points of law as set forth by him:—

“(i) After the notice under section 22 (4) had been served and in compliance therewith the assessee appeared with the accounts called for, the force of the notice under section 22 (2) disappeared (Assistant Commissioner of Income-tax, Cawnpore, in his appellate order admits this)

(ii) The Income-tax Officer could assess the petitioner under section 23 (4) immediately after the non-compliance of notice under section 22 (2) without going into elaborate proceedings of section 22 (4). But when subsequently a notice under section 22 (4)

was issued and was duly and completely complied with, the Income-tax Officer was debarred from making an assessment under section 23 (4) without definitely declaring the accounts as false or *farzi*, and his action in assessing the petitioner under section 23 (4) was unfair and bad in law.

- (iii) When accounts were produced in compliance with notice under section 22 (4) and prunts could have been worked out in no time, according to the views expressed by the Income-tax Officer in his order, it was unjust and unfair for him not to go into the actual accounts of prunts and in framing the assessment on purely guess work, more so because he did not reject them on the ground that income, profits and gains could not be properly deduced therefrom as laid down in section 13.
- (iv) When the Income-tax Officer did not go through the complete accounts it was unjust and unfair for him to say that income from cotton speculation business was not entered therein, and when questioned to say that he could not examine full accounts within the time at his disposal, and it was still more unlawful and unjust to have over-sacked the petitioner for his (Income-tax Officer's) own action.
- (v) When petitioner attended the Income-tax Officer's court in compliance with notice under section 22 (4) and the force of the notice under section 22 (2) had disappeared, there is no provision in the law to ask the petitioner at that stage to file a return of income or the alleged default in doing so to lead an assessment under section 23 (4).
- (vi) As a reason for rejecting the application under section 27, the Income-tax Officer noted "the question whether five days were sufficient or not does not arise. The law provides no procedure for extension of time over one month except in first instance." Under the ordinary practice, procedure and courtesy of Courts of Law and in the sense of equity and justice the order passed was a tall order and in the circumstances that two medical certificates were filed any court would have granted one more extension of time for the petitioner to prove his *bona fides* in the matter, or at least to bring him within the four corners of law.
- (vii) Was the serious illness of a female member of the joint Hindu family which involved male members into perplexity and anxiety, and petitioner's illness from tooth-ache, certified by the Civil Surgeon, not sufficient cause for the purposes of section 27 or adequate reason for granting further extension of time?
- (viii) To send for the accounts for the last two years during the proceedings under section 27 was illegal, and still more illegal it was then when they were sent for and produced they were not utilized as documentary evidence in support of petition under section 27.
- (ix) The appellate authority for reasons stated above erred in agreeing with the Income-tax Officer's finding that 'there was no adequate reason in this case for non-compliance with notice under section 22 (2)'. When proceedings under section 22 (4) was initiated, it was bad in law to have dealt with the appeal and rejected it on the ground of non-compliance of notice under section 22 (2) alone.

without dealing with the proceedings under section 22 (4). The whole appellate order is defective and bad in law."

4. Points (ii), (iii) and (iv) relate to the method of assessment and do not arise out of proceedings relating to section 27. The Commissioner is unable to state a case on these questions.

The first and fifth points arise out of a misinterpretation of the language used by the Assistant Commissioner when he said that on May 28, 1928, "there was no notice under section 22 (2) in force for the compliance with which the Income-tax Officer could give the appellant an extension of the date." The meaning of this sentence, as is clear from the rest of the order, was that the time fixed in the notice under section 22 (2) had expired, and that there was no provision in the Act by which an Income-tax Officer could extend the date originally fixed. He did not mean that the notice under section 22 (2) had become of no effect and that therefore the provisions of section 23 (4) had ceased to have force. No question of law arises in this connexion.

The sixth point is based on a misapprehension. The point in issue is the failure of the assessee to file a return on or before May 12, 1928, and not his inability to make use of the provisions of section 22 (3). The seventh point gives the reasons for this inability. No point of law, in the Commissioner's opinion, can be considered to arise here.

The eighth point is irrelevant.

Point (ix) appears to be the same as point (ii), in effect.

The Commissioner is thus unable to state a case on the questions of law propounded by the assessee. The only point which arises, and can arise, is:— Was the assessee prevented by sufficient cause from making the return required by section 22?

The petitioner failed to raise this question clearly, either in his petition to the Income-tax Officer under section 27, or in the grounds. But in the circumstances of the case the Commissioner states it for the decision of the High Court.

5. The Commissioner is of opinion that the answer is in the negative for the ample reasons given in the assessment order, viz., that when the assessee produced his books they were in such a state that they could have been completed in a very short period of time, and there was no real difficulty on this score.

6. Paragraphs 1 to 4 were sent to the petitioner for observations and representation, if any, and a copy of his representation is attached as appendix H. I do not consider it necessary to make any addition or alteration.

JUDGMENT.

This is a statement of the case by the Commissioner of Income-tax under section 66 (2) of the Indian Income-tax Act, 1922.

The facts are given in the statement and very briefly are these. There is a joint Hindu family of which Lala Kalyanmal seems to be the head. He was called upon by the Income-tax Officer to furnish a return of the income by a notice which was served on Lala Kalyanmal on 13th April 1928. The notice was under Sec. 22 (2) of the Act and called upon the proposed assessee to make his

return of income by 12th May 1928. It will be noticed here, for this is a very important matter, that the proposed assessee had only 29 days within which to comply with the order. Kalyanmal failed to comply with the order and on 19th May 1928, the Income-tax Officer called on Lala Kalyanmal, by means of a notice issued under Sec. 22 (4) to submit his account books on 28th May 1928. On that date, Lala Kalyanmal did appear with the accounts books. He was able to persuade the Income-tax Officer to grant him 5 days' more time to file a return of his income. Time was granted up to 2nd June 1928. On that date, Lala Kalyanmal did not turn up, nor did he furnish any return of the income. What he did however, was that he sent a Civil Surgeon's certificate to the effect that his son had left Cawnpore, because his (son's) wife was suffering from consumption and that he himself was suffering from a toothache. His application was disallowed and on 2nd June 1928, an assessment to the best of the judgment was made by the Income-tax Officer under the provisions of Sec. 23 (4) of the Act.

Lala Kalyanmal thereupon made an application to the Income-tax Officer to give him a fresh opportunity to file his return. His application was made under Sec. 27 of the Act. It was rejected by the Income-tax Officer and an appeal to the Assistant Commissioner of Income-tax was also rejected by that Officer. Lala Kalyanmal thereupon made an application to the Commissioner of Income-tax to state the case to this Court. Lala Kalyanmal formulated 9 questions of, what he thought were, points of law. The learned Commissioner has stated those points in the statement of the case and has remarked that these questions were either questions of fact, or they did not arise at all. One of the questions, namely 7 was in the following language:—"Was the serious illness of a female member of the joint Hindu family which involved male members into perplexity and anxiety, and petitioner's illness from toothache..... not sufficient cause for the purpose of Sec. 27 or adequate reason for granting further extension of time?"

As regards this point, the Commissioner was of opinion that it was a question of fact and not a question of law. Having however said so much, the learned Commissioner formulated the following question for determination by this Court:—"Was the assessee prevented by sufficient cause from making the return required by Sec. 22?"

The question as framed by the learned Commissioner is a mixed question of fact and law, but the question of law can be answered only when the facts have been determined. If the facts be as is stated in question 7 formulated by Lala Kalyanmal and if those facts be accepted as true, then a question might arise, whether those facts might be treated as a sufficient cause in law, within the meaning of Sec. 27 of the Act. We find that the Commissioner himself, the Assistant Commissioner of Income-tax and the Income-tax Officer, have all discredited the allegation as to illness and as to whether the alleged facts prevented any interruption of Lala Kalyanmal's business. In the circumstances, we are of opinion that no question of law, as framed, arises in the case.

Having however said so much, we have found that there is a very substantial question of law raised in the statement of the case. We have already held, in another case, that it is open to the High Court to formulate questions of law that really arise in a case and to answer them for the benefit of the Commissioner and the parties.* The substantial question of law that arises in this case is whether the notice that was issued to Kalyanmal under Sec. 22 (2) of the Act was at all a legal notice? Under that rule of law, the Income-tax Officer must give the proposed assessee at least 30 days' time within which to file a return. Even this minimum was denied to Lala Kalyanmal and in our opinion, the notice

* See *Siva Prasad Gupta v. Commr. of Income-tax, U. P.* at page 406 *infra*.

was entirely illegal. The fact that subsequently 5 days' time was granted to Lala Kalyanmal (from 28th May 1928 to 2nd June 1928) will not cure the defect that initially lay in the notice issued. Our opinion is that the notice issued being illegal, there could possibly be no valid assessment of income-tax under Sec. 23 (4).

We may mention here that we have heard the learned Government Advocate on the point and our decision has been arrived at after hearing him on this point. We direct that a copy of this opinion be sent under the seal of the Court to the Commissioner of Income-tax. We direct that the parties pay their own costs, in view of the fact that this point, namely the illegality of the notice, was never raised before. We allow the Government Advocate to file a certificate of fees for Rs. 100 within the allotted period of 30 days.

(302) IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Mr. Justice Tek Chand and Mr. Justice Aga Haidar.

(8th April, 1929).

Messrs. Karam Ilahi Muhammad Shafi

Assessee.*

v.

The Commissioner of Income-tax, Delhi

Referring Officer.

Income-tax Act (XI of 1922), Secs. 10 (2) (vi) & 24—Depreciation allowance—No profits in business using machinery, etc., depreciating—"Profits or gains" in proviso, meaning of.

An assessee is entitled to the depreciation allowance under Sec. 10 (2) (vi) of the Income-tax Act in a year when there are no profits or gains in the business using the machinery, etc., depreciating and can set off this allowance under Sec. 24 against his profits and gains from other sources, such as rentals from house property, during the year in question.

"Profits or gains" in proviso 2 to Sec. 10 (2) (vi) are profits or gains generally from whatever source derived and are not confined to the profits or gains of the particular business alone in which the buildings and machinery, etc., are used.

Case (Reference No. 31 of 1927), stated under Sec. 66 (2) of the Indian Income-tax Act, (XI of 1922), by the Chief Commissioner, Delhi, for the opinion of the High Court.

CASE.

The point at issue in this case is stated in paragraphs 2 and 3 of the application before me. Can depreciation on buildings and machinery be set off against gains or profits accrued to the owner of these buildings and machinery from other sources, such as rental from house property?

The question is simple enough, but decisions on the point are conflicting. The point arose in connection with the assessment of the applicant for 1925-26

* A. I. R. (1929) Lah. 556.

and was decided in appeal in favour of the applicant by the Assistant Commissioner in his order dated 27th August 1926. The point was brought to my notice, and I proceeded to review the Assistant Commissioner's order. After hearing the applicant I decided against him in my order dated 3rd June 1927. After hearing Mr. Abdur Rahman for the applicant in regard to this year's assessment I see no reason to alter the opinion arrived at in my order quoted above.

I have been asked to refer the case to the High Court, and as I am aware that the point at issue in this application is the subject of considerable controversy I decide to do this. My views on the point have already been stated in my order in the former revision application dated 3rd June 1927.

Dr. Moti Sagar and Bisham Narian, for the Assesseees.

C. H. Carden Noad, for the Crown.

JUDGMENT.

In order to understand clearly the point of law involved in this reference, it is necessary to state the following facts which are admitted as correct by counsel on both sides. The assessee, Messrs. Karam Ilahi Muhammad Shafi of Delhi had in the accounting period in question three different sources of income:— (a) rent from house property at Delhi, (b) business of oilman's stores, etc., in Saddar Bazar, Delhi, and, (c) business known as Rahman Ice Factory, Delhi.

The assessee submitted a return showing profits in (a) but losses in (b) and (c) and claimed to set off the latter against the former. The Income-tax Officer admitted the claim so far as the loss in (b) was concerned and there is now no dispute with regard to it. He, however, refused to allow the set off in respect of the alleged 'loss' in Rahman Ice Factory, (c), in so far as it consisted of depreciation of buildings and machinery, which the assessee claimed to deduct under sub-clause (vi) of section 10 (2) of the Act. This order was upheld on appeal by the Assistant Commissioner and on review by the Commissioner who held that under the Act, this allowance was permissible only if there had been actual gain or profit under *this particular head of business*, i.e., the Rahman Ice Factory in the year in question, and that failing such income the proper procedure under proviso (b) to sub-clause (vi) of section 10 (2) was to carry over the depreciation to succeeding years, until there were sufficient profits from this particular business, against which alone it could be set off. On the application of the assessee the Commissioner has, however, referred the following question to this Court for decision under section 66:—“Can depreciation on buildings and machinery be set off against gains and profits accrued to the owner of those buildings and machinery from other sources, such as rental from house property?”

The decision of the question depends on the interpretation of sections 6, 10, and 24 (1) of the Income-tax Act. Section 6 enumerates the various heads of income, profits and gains chargeable to income-tax. Of these we are concerned in this case with heads (iii) and (iv), i.e., “Property” and “Business” only. Section 24 (i) lays down that where any assessee sustains a “loss of profits or gains in any year under any of the heads mentioned in Sec. 6, he shall be entitled to have the amount of the loss set off against his income, profits or gains under any other head in that year.” The loss of profits or gains under “Business” can, therefore, be set off against the income from rental on property.

Sec. 10 provides the mode of computing “profits or gains” under the head “business”. Sub-section (1) of this section is to the effect that the tax

shall be payable by an assessee under the head "Business" in respect of the profits or gains of *any* business carried on by him. It has been ruled by the Madras High Court that the word 'any' in this clause means "each and every business" and not merely each business separately *Commissioner of Income-tax v. M. Ar. Ar. Arunachalam Chettiar*(1), and this ruling has been followed in this Court. It may, therefore, be taken as settled law that if a person carries on two or more distinct businesses, the profits or losses of all of them are to be added together, and the aggregate sum so arrived at represents his "profits or gains" under the head "Business". If the net result of this calculation shows a loss, such loss may under Sec. 24, be set off against the profits or gains derived by the assessee from other heads of income in that year.

According to sub-section (2) of section 10 the "profits or gains" under each head of business are to be computed after making certain allowances which are enumerated therein. It is conceded by the learned Government Advocate that if after deducting the allowances described in clauses (i) to (v), (viii) and (ix) of this sub-section there is a net loss in a particular business such loss can be adjusted against the profits in another business as well as against profits or gains under other sources of income. But he contends that a different rule must be followed in respect of the allowances mentioned in clauses (vi) and (vii) inasmuch as they are in the nature of depreciation of capital and unless there is a profit in that *particular business* in the year in question they cannot be taken into account.

After carefully examining the provisions of the Act, I find myself unable to accept this contention as correct. Section 10 makes no such distinction among the various kinds of allowances to which an assessee is held entitled, and there is no justification for treating the allowances described in clauses (vi) and (vii) differently from those mentioned in the other clauses of the sub-section. It is no doubt true that these allowances do not represent actual payments made by the assessee during the year, but the Legislature has expressly permitted the assessee to deduct every year a certain percentage of his outlay on buildings and machinery before his assessable income can be ascertained, and in the absence of clear and explicit words to the contrary I can see no reason for holding that this allowance can be claimed only if sufficient profits have accrued in the particular business in which the machinery and buildings were used.

For the respondent reliance is placed principally on proviso (b) to clause (vi) which runs as follows:—

"Provided that—

• • • • • •

(b) where full effect cannot be given to any such allowance in any year owing to their being no profits or gains chargeable for that year, or owing to the profits or gains chargeable being less than the allowance, the allowance or part of the allowance to which effect has not been given, as the case may be, shall be added to the amount of the allowance for depreciation for the following year and deemed to be part of that allowance, or, if there is no such allowance for that year, be deemed to be the allowance for that year, and so on for succeeding years." This proviso, however, if construed according to its plain wording, cannot possibly bear the construction sought to be put on it on behalf of the Crown. The learned Government Advocate has very fairly and

(1) 1 I. T. C. 273.

properly conceded that this interpretation is possible only if the words "no profits or gains" are read as meaning "no profits or gains of the particular business of which the financial results are being computed." But I do not find any warrant for importing in the clear and explicit phraseology used in the statute the additional words suggested on behalf of the respondent. Reading the proviso in its plain meaning and interpreting it according to well-settled canons of construction of fiscal statutes, I have no hesitation in holding that the 'profits or gains' referred to above are profits or gains generally from whatsoever source derived and are not confined to profits or gains of the particular business alone in which the buildings and machinery were used. I have no doubt that the provision for carrying over the unabsorbed depreciation allowance to the succeeding years is not the exclusive remedy allowed to the assessee and cannot be interpreted as debarring him from claiming the benefit of the earlier part of the subsection.

My answer to the question referred to this Court therefore, is that under sub-clause (vi) of section 10 (2) depreciation on buildings and machinery can be set off against gains and profits accrued to the owner of those buildings and machinery from other sources such as rental from house property during the year in question.

Having regard to all the circumstances, I would leave the parties to bear their own costs of these proceedings in this Court.

The announcement of this judgment has been delayed as after arguments in this case had been heard and judgment reserved, it was represented to me that the question involved in this reference had been considered and decided by a Full Bench of the Madras High Court in a case which had not yet been reported and that I should consult that decision before passing orders. I have since had the advantage of perusing the Madras judgment* but am disappointed to find that it dealt with a totally different point, which had no bearing whatsoever on the question before us.

AGHA HAIDAR, J.:—I agree.

(303) IN THE COURT OF THE JUDICIAL COMMISSIONER, NAGPUR.

Before Mr. Mohiuddin and Mr. Subhedar, Additional Judicial Commissioners.

(15th April, 1929).

Jambudas Devidas Chawre

.. Assessee.

v.

The Commissioner of Income-tax, Central Provinces and Berar.

.. Referring Officer.

Income-tax Act, (XI of 1922), Sec. 66—Sufficiency of evidence, when a question of law—Findings of fact, jurisdiction to revise.

SEMBLE. Where on the evidence only one legal inference is alone possible and that has not been drawn, a question of law arises.

* The case referred to is *Messrs. Massey & Co., Ltd., v. Commissioner of Income-tax, Madras* reported at page 802 *infra* Ed.

If one of two possible inferences is drawn by a court which is the final authority on facts, no question of law arises in the case.

Case (Misc. Judicial Case No. 46-B of 1927), stated under Sec. 66 (3) of the Indian Income-tax Act, (XI of 1922), by the Commissioner of Income-tax, Central Provinces and Berar, for the opinion of the High Court.

CASE

For the assessment during the year 1925-26, Jambudas Devidas Chawre of Karanja in the Akola District, returned an income of Rs. 23,151-5-0, as having been made during the year ending in Diwali 1924 (28th October 1924). This return was not accepted and his books of accounts were seen and the total taxable income was found to be Rs. 43,361. In this income was included an item of Rs. 15,400 said to have been made as interest on the decree passed against Sheikh Amir and others of Karanja. The Assistant Commissioner who made the assessment in this case levied a penalty under section 28 on this item at the maximum rate. Appeals against the assessment and against the penalty imposed were made to me. Both the appeals were rejected on the 9th July 1926. An application under section 66 (2) was then made to me on the 9th August 1926, to refer the case to the High Court. It did not clearly set forth the point for consideration. Hence another application, dated the 2nd September 1926, clearly stating the points for reference was put up. Thus the point for reference now is:—“Under the circumstances of the case and in view of the system of book-keeping observed by the assessee, was the Income-tax department justified in holding that the assessee was guilty of concealment of income within the meaning of section 28 of the Income-tax Act and that he was liable to be penalised with the maximum penalty with respect to the item of Rs. 15,400?” For reasons given in my order dated the 23rd September 1926, I held that no question of law arose and reference to the High Court was not made. The assessee then moved the High Court under section 66 (3) of the Income-tax Act and under the orders of the Additional Judicial Commissioner, dated the 15th July 1927, I am required to state the case. In compliance with it, the case is submitted for favour of the decision of the Hon'ble the High Court.

2. The question has got 4 component parts:—(1) Whether under the circumstances of the case (2) and in view of the system of book-keeping observed by the assessee (3) the Income-tax Department was justified in holding the assessee guilty of concealment of income within the meaning of section 28 of the Income-tax Act and (4) and holding him liable to be penalised with maximum penalty. I beg to discuss all these four points as below.

3 *As regards the circumstances of the case.*—When Jambudas Devidas Chawre made the return under section 22 (2) of the Income-tax Act, he enclosed with it a statement showing how he arrived at the taxable profits. This was done as required by Note 5 (b) of the printed notes in this return, *vide* Rule 19 of the Rules framed under the Income-tax Act. According to this note details of the gross receipts and expenditure have to be given. The item of Rs. 21,400 received from Sheikh Amir and others on the 15th February 1924 should have also been shown here; but it was not. Nor was it shown in the enclosure. The examination of accounts showed that this item was not entered in the accounts of Sheikh Amir and others at all. The Income-tax Officer while surveying the town of Karanja had come to know of this payment during his survey enquiries. He writes as follows:—“It was ascertained while performing advance survey of this assessee that he received full satisfaction of the decree in Suit No. 16[21 in Second Additional District Judge's Court, Akola. Assessee's debtor called Sheikh Amir

mohammad of Karanja was compelled to sell several of his shops in Kachi Bazar at Karanja to Motilal Onkarsa Chawre of Karanja, to liquidate this decree. Assessee's pleader in this case was Mr. J. D. Chawre of Akola. Now I find on page 127 ledger and 52 Rokad of assessee's account that he has credited Rs. 21,400 in Ravangi Khata. The Khata of the debtor whose original amount of loan was only Rs. 6,000 is found carried forward to Samvat 1981 with a net debit of Rs. 7,146-1-0." It was therefore necessary for him to ascertain as to what became of this big item of income. He examined Hirusa Laxmansa, the agent of the applicant, and this agent admitted; "That Rs. 21,400 are received by us from Sheikh Amir Lalmohammad of our town from Akola Court. We have appealed to the Third Judicial Commissioner's Court, Nagpur, against the asami and Motilal Chawre that Rs. 21,400 is insufficient to cover our interest. We think that some Rs. 4,000 might be more for interest. I admit that the original loan was of Rs. 6,000 which grew to Rs. 7,146-1-0 at the end of the account year when expenses were tacked. We shall show interest when appeal is decided." In the written grounds of appeal, the explanation given for omitting this item was "Rs. 15,400 for interest. This had to be shown in a sort of suspense account as the matter was pending decision in the Court of the Judicial Commissioner at Nagpur." This second explanation for the omission of a big item was therefore an improvement over the previous one. Then the examination of accounts disclosed that the receipt of this item was not entered in the Khata of Sheikh Amir of Karanja which was the proper place. It was detected as entered in the Ravangi Khata. This Khata, as the name implies, deals with cash advanced to servants at the time of their departure (Ravangi) to Akola to meet Court and other expenses. The account of these advances are taken from servants on their return to Karanja and are entered in this Khata (Ledger). The amount of Rs. 21,400 was not such an item. It should not have been entered in the Ravangi Khata. Even in the Ravangi Khata the item is not shown as having been received from Sheikh Amir. It is entered as "Rs. 21,400. Cash through Devidas Ruiwalla." If the item was to be treated as part payment, then too the proper place for it to be entered was Sheikh Amir's account and for interest, (Rs. 21,400 minus Rs. 6,000, i.e., Rs. 15,400) the Kasar of Interest Khata. Then mention of this amount should have been made in the enclosure to the return under section 22 as stated above.

4. *As regards the system of book-keeping.*—It is admitted that the applicant follows the cash system of accountancy, i.e., as soon as the money is received or issued in cash it is entered into the books of accounts. Under this system, therefore, the receipt of Rs. 21,400, should have been entered in its proper place, i.e., in Sheikh Amir's Khata and the net interest of it, i.e., Rs. 15,400 entered into the Kasar Khata, i.e., Interest Account. This, as shown above, was not done, though with the system of accountancy obtaining with the assessee it should have been.

5. *The Income-tax Department was justified in holding, etc.*—I beg to submit that the principle of the normal presumption being in favour of the assessee's good faith does not seem to have been departed from in this case. The facts of the case as given above clearly show that the applicant (assessee) has not been acting in good faith. On the 11th February 1924, his counsel and brother Mr. Jaikumar Devidas Chawre, practising as pleader at Akola, drew this money from Civil Courts and passed it on to the assessee at Karanja. The money was not shown as having been received from Sheikh Amir and other debtors through Mr. J. D. Chawre. It was entered in Ravangi Khata which is not the place for such amounts, and not in Sheikh Amir's Khata. The interest was not entered in Interest Khata as the system of accounts in question required. No mention of this item of receipt being omitted or held in suspense was made in the return

under section 22 or its enclosure. But for the personal information of the Income-tax Officer the receipt of this amount would not have come to light. It was not a small item to have been forgotten by the applicant. On the other hand it was a good single item of interest to be kept back from the Department. Under these circumstances of the case, I submit the Income-tax Officer had very good reasons to be satisfied that the applicant had concealed the particulars of his income or had deliberately furnished inaccurate particulars of it and had returned it below its real amount, and to impose penalty under section 28 (1) of the Income-tax Act.

6. *As regards the maximum penalty*:—I submit that section 28 of the Income-tax Act gives full discretion in this matter to the Income-tax Officer and having regard to the facts of the case, it appears to me that he has exercised his discretion very reasonably

7. In conclusion, I submit that this question be answered in the affirmative.

W. R. Puranik, for the Assessee.

D. N. Choudhary, for the Crown.

JUDGMENT.

The facts necessary for the disposal of this reference are shortly these. In the assessment proceedings for the year 1925-26 the assessee, Jambudas Devidas of Karanja, submitted a return under section 22 (2) of the Income-tax Act on the usual form and appended to it a schedule, as required by rule 19 of the rules framed under the said Act, showing his total taxable income as Rs. 23,151-5-0, for the one year ending the Divali of 1924. This return was not accepted and therefore after an examination of his books of accounts the Assistant Commissioner of Income-tax found his income to have been Rs. 43,361 inclusive of an item of Rs. 15,400 representing interest, received by the assessee through the Civil Court, in respect of a decretal debt due from Sheikh Amir and others. The assessee was accordingly assessed to income-tax on the aforesaid income and the Assistant Commissioner, who made the assessment in the case, also levied a penalty under section 28 of the Income-tax Act on the amount of Rs. 15,400 at the maximum rate, holding that the assessee was guilty of "deliberate concealment" of this part of his income. The Commissioner of Income-tax to whom an appeal was preferred also concurred with this finding of the Assistant Commissioner and held that the penalty was correctly imposed. After the dismissal of his appeal the assessee unsuccessfully moved the Commissioner, under section 66 (2) of the Income-tax Act, to refer the point in dispute for the decision of this Court and later on filed an application in this Court under section 66 (3), *ibid*, which was allowed by Kinkhede, A. J. C., who directed the Commissioner of Income-tax to make the desired reference (Miscellaneous Judicial Case No. 44-B of 1926, dated 15-7-1927).

2. It is in obedience to this mandamus that the Commissioner of Income-tax has made the present reference for the decision of the following point:—

"Under the circumstances of the case and in view of the system of book-keeping observed at the assessee's, was the Income-tax Department justified in holding that the assessee was guilty of concealment of income within the meaning of section 28 of the Income-tax Act and that he was liable to be penalised with the maximum penalty with respect to the item of Rs. 15,400?"

3. For the proper decision of the question referred to us it is necessary in the first instance to recapitulate the facts found, in this case, by the Income-tax authorities. These are briefly as under:—(a) that on 22-6-1925, the assessee filed his return on the usual form and attached thereto a schedule showing how he arrived at the figure of taxable profits; (b) that the item of Rs. 15,400 representing the amount of interest, which is the subject in respect of which penalty has been imposed, was not shown by the assessee in the aforesaid schedule; (c) that the assessee follows the cash system of accountancy, i.e., as soon as the money is received or issued in cash it is entered in the books of accounts. Under this system, therefore, the receipt of Rs. 21,400 should have been entered in its proper place, i.e., in Sheikh Amir's Khata, and the net interest of it, i.e., Rs. 15,400 entered into the Kasar Khata, i.e., interest account. This was not done though, with the system of accountancy obtaining with the assessee, it should have been; (d) that the assessee had, as a matter of fact, withdrawn the amount of Rs. 21,400 (inclusive of the sum of Rs. 15,400 for interest) from the Civil Court deposit on 11-2-1924. He credited it in his cash book on 15-2-1924 and posted it immediately in the "Ravangi Khata" against the name of his brother Mr. Jaikunnar, Pleader, who had actually withdrawn the amount at Akola and sent it on to the assessee at Karanja; (e) that the assessee did not, along with his return, submit any explanation as to why this amount was not shown therein as income in the account year; (f) that long before the return was submitted by the assessee, the Income-tax Officer in his prospective survey operations had come to know that the assessee had received this large amount in satisfaction of the decree; (g) that the assessee did not of his own accord submit his books of account for the inspection of the Income-tax Officer in support of his return; (h) that when the books of accounts were produced in obedience to the order of the Income-tax Officer and he discovered this large amount credited therein and called upon the assessee to explain why it was not included in the return, Hirusa, the agent of the assessee, simply stated that because an appeal was preferred against the decree claiming the additional sum of about Rs. 4,000 "the amount of interest would be shown in the accounts after the appeal was decided." In the written grounds of appeal before the Commissioner the reason assigned for the omission was that "the amount of Rs. 15,400 for interest had to be shown in a sort of suspense account as the matter was pending decision in appeal." (i) that the Income-tax authorities also discovered that there was no other instance in which payments received in satisfaction of decretal debts were ever posted in the "Ravangi Khata" by the assessee; (j) that the "Ravangi Khata" meant and dealt only with the items that are issued in cash by the owner of the shop to his servants for Court and other expenses and which are adjusted as soon as the servants return to the head-quarters and that Rs. 21,400 in question was admittedly not a remittance so sent out by the assessee; and (k) that but for the inspection of the account books by the Income-tax Officer, which was prompted by the knowledge he had already gained in his survey enquiries, the item in question would have remained concealed from the income-tax authorities.

4. It was upon these facts that the Assistant Commissioner as well as the Commissioner of Income-tax came to the conclusion that the assessee's conduct came within the purview of section 28 (1) of the Income-tax Act which states that "If the Income-tax Officer . . . is satisfied that an assessee has concealed the particulars of his income, or has deliberately furnished inaccurate particulars of such income, and has thereby returned it below its real amount, he may direct that the assessee shall, in addition to the income-tax payable by him, pay by way of penalty a sum not exceeding the amount of income-tax which would have been avoided if the income so returned by the assessee had been accepted as the correct income." The learned Commissioner of Income-tax in paragraph 5 of the reference assures this Court that the principle of the normal

presumption being in favour of the assessee's good faith was not departed from in this case in arriving at the aforesaid finding.

5. In issuing the mandamus our learned brother Kinkhede, A. J. C., had observed that "The question whether the applicant has been rightly found to have concealed his income from the Income-tax Department depends upon the decision of the question whether or not, on the facts found the inference of concealment could be based", because according to the dictum of their Lordships of the Privy Council in *Nafar Chandra Pal v. Shukur*(1), "the proper legal effect of proved facts is a question of law."

6. Mr. Puranik, the learned Advocate for the assessee, pressed upon us to review the adverse finding of the Income-tax authorities on the ground that the only inference that could legally be drawn from the facts ascertained in the present case was that there was no intention on the part of the assessee to conceal his income or deliberately make an inaccurate return thereof, however negligent or unbusinesslike the conduct of the assessee may have been in not maintaining his accounts properly, which may possibly have resulted in the return being inaccurate in respect of the item of Rs. 15,400. It was not, and could not be denied that the receipt of the amount in question during the assessment year was a part of the total taxable income for that year. It was however contended that at the time when the return was submitted the assessee honestly believed that it was not an income accrued during the year because he had not appropriated it as such in his accounts, though it may be, that he should have done so.

7. On the other hand, Rai Bahadur D. N. Choudhry, who appeared for the Commissioner of Income-tax, contended that one and only one conclusion could not be drawn from the facts found and that it was as much possible to draw the inference of innocence or mistake suggested for the assessee, as the one to the contrary already come to concurrently by the two responsible officers of the Income-tax Department. It was, therefore, argued that no question of law arose in the case for decision.

8. In view of the authorities noticed in the following paragraphs we have no hesitation in holding that the finding of the Income-tax authorities that the conduct of the assessee came within the purview of section 28 of the Income-tax Act was a pure finding of fact which is not open to revision by this Court.

9. In *Rajaram v. Ganesh*(2), it was observed:—"From facts found it is often easy to rule with certainty that a certain legal inference ought or ought not to be drawn. When such a state of facts occurs, the Court in second appeal can and often does correct erroneous conclusions drawn by the lower appellate Court. Where, however, the legal inference to be deduced from facts is doubtful, it is not open to this Court in second appeal to interfere with the findings of the lower Court. A test which often presents itself to an English lawyer is this:—Would a Judge withdraw the case from a jury on the ground that there was no evidence of the question to be found upon, such as adverse possession or title, to go to them, or would he, on the other hand, on certain facts being established, direct them to find in a particular manner? In either of these cases it would be open to this Court in second appeal to come to a different conclusion from the lower appellate Court. But where the question upon the facts and law is

(1) 46 Cal. 189 (P. C.) at 195.

(2) J. L. R. 21, Bom. 91.

one which the Judge would lay before the jury to decide, there it is not open to this Court to consider the propriety of the finding of the lower appellate Court."

10. In *Madho v. Govindbhat*(1), Drake-Brockman, J. C., followed the principle enunciated in the aforesaid Bombay case and held that where more than one inference is open the High Court can not in second appeal refuse to be bound by that drawn in the Court below. Similarly in *Mt. Mathurabai v. Lalsingh*(2), Kinkhede, A. J. C., approved the view propounded in the Bombay case and observed that the mere fact that a Court of appeal draws one of two possible inferences on a question of fact does not entitle the second appellate Court to interfere with the finding based upon such inference and that it is only where one legal inference is possible and which has not been drawn that interference is justified. Again, in *E. I. Railway Co. v. Badrilal*(3), the same learned Judge laid down the law in these words:—"Given certain set of facts, from which two inferences are possible it is open to the first appellate Court to draw any one of them, vide *Rajaram v. Ganesh Hari Karkhanis*(4), and his decision will not be open to challenge in second appeal. Their Lordships of the Privy Council discountenanced the practice of undue interference in second appeal with findings of facts duly supported by evidence proper for consideration. They have expressed their disapprobation in the following passage of their judgment in *Nafar Chandra Pal v. Shakur Shaikh*(5). The mere fact 'that upon the documents and evidence placed before the learned District Judge the High Court would have come to a different conclusion' is no ground for second appeal; it is precisely this revision of evidence which is excluded by the limited character of a second appeal. In *East Indian Railway Company v. Changa Khan*(6), it was held that after there has been a decision of fact in the two Courts of original and first appellate jurisdiction the High Court cannot entertain a second appeal upon any question as to the soundness of findings of fact by the lower Appellate Court. If there is evidence to be considered the decision of the second Court, however unsatisfactory it might be when examined, must stand final."

11. The application of the rule deducible from the above authorities makes it perfectly clear to us that on the facts found in the present case no question of law arises for our decision. It is also equally clear to us that if it were possible for us to review the findings we would have come to the same conclusion upon the facts established in the case as has been come to by the Income-tax authorities. We, therefore, answer the reference in the affirmative. The assessee shall pay the costs of this reference. Counsel's fee Rs. 100.

(304) IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Mr. Justice Tek Chand and Mr. Justice Aga Haidar.
(15th April, 1929).

Messrs. Chunna Mal Salig Ram

v.

.. Assessee.*

The Commissioner of Income-tax, Delhi

.. Referring Officer.

Income-tax Act (XI of 1922), Sec. 9 (2)—Annual value of house property—Municipal tax, if included therein—Delhi Municipal Committee.

(1) 46 Ind. Cas. 794.

(2) 78 Ind. Cas. 112.

(3) 90 Ind. Cas. 209.

* A. I. R. (1929) Lah. 503.

(4) 1. L. R. 21 Bom. 91.

(5) 1. L. R. 46 Cal. 189.

(6) 1. L. R. 42 Cal. 888.

The expression 'annual value' in Sec. 9 (2) of the Income-tax Act does not include house-tax levied on the landlord by the Municipal Committee under the Punjab Municipal Act.

Case (Reference No. 34 of 1928), stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922), by the Chief Commissioner, Delhi, for the opinion of the High Court.

CASE.

This is a petition from Messrs. Chunna Mal Salig Ram under Sec. 66 (2) of the Income-tax Act, requiring me to make a reference to the High Court on a point of law, viz., whether the annual value of a building under Sec. 9 (2) of the Act includes the house tax levied by a Municipal Committee or not.

Mr. Abdur Rahman who appears for the petitioners states that he is not claiming a deduction from the rent on account of house tax. What he claims is that the house tax and the rent are two entirely different things and that the addition of the former to the latter to make up "annual value" for the purposes of section 9 (2) of the Income-tax Act is unauthorised. In support of this argument he relies mainly on paragraph 28 of the Income-tax Manual, Volume I, which says that "the *bona fide* annual value of a building is the full market value at which the building could be let from year to year irrespective of any charges by way of municipal rates or taxes thereon." This sentence is no doubt ambiguous but its meaning is made clear by the sentence which follows:—"It therefore differs from.....actual rent payable on a yearly lease.....with tenant's liability to pay owners rates or taxes". From this it seems to follow that the sum for which the property might reasonably be expected to let from year to year is to be taken as including any rates and taxes payable under law by the owner such as the tax on buildings under section 61 (1) (a) of the Punjab Municipal Act.

Mr. Abdur Rahman also relies on explanation II to section 3 (1) (b) of the Punjab Municipal Act which states that the term "gross annual rent" shall not include any tax payable by the owner in respect of which the owner and tenant have agreed that it shall be paid by the tenant. As regards this argument I need only observe that a comparison of section 63 of the Punjab Municipal Act with section 9 of the Income-tax Act shows that the calculations of annual value are not made in the same manner for the purposes of the two Acts. It would not therefore be safe to assume that the explanation in question could be read as applying by analogy to the Income-tax Act.

Apart from this I do not understand that the petitioners contend that there has been any specific agreement on the lines of the explanation in question by which the tenants have bound themselves to pay the house tax. It is perhaps curious that there should apparently be no recorded ruling on the point which has been raised, but I find it a little difficult to believe that if the Legislature had intended that house tax should not be regarded as a part of the rent in a case like the present, or that a deduction should be allowed on account of it they would have made their meaning clear. Section 9 (1) (v) leaves no doubt in regard to land revenue.

For the above reasons it is my opinion that the house tax is not an addition to the rent but is part of the rent and with this expression of my opinion I forward the case to the High Court of Judicature at Lahore as required by section 66 (2) of the Act.

R. B. Lala Badri Das, for the Assesseees.

Carden Noad, for the Crown.

JUDGMENT.

AGHA HAIDAR, J.:—This is a reference by the Commissioner of Income-tax, Delhi, under Sec. 66 (2) of the Indian Income-tax Act, (Act XI of 1922). The point involved in this reference is a short one and may be stated as follows:—

Messrs. Chunna Mal Salig Ram of Chandni Chowk, Delhi, are extensive owners of house property. The Municipal Committee, Delhi, has imposed upon them a house tax of Rs. 6,760. This has been added by the Income-tax Officer to their income derived from house-rents, which amounts to Rs. 2,47,349. This amount of the house tax actually realised by the assessee in the year in question came to Rs. 5,543|- only. The question is whether Messrs. Chunna Mal Salig Ram should be assessed to income-tax on their annual rental Rs. 2,47,349, or upon the total of the two items, namely, the annual rental plus the house tax Rs. 2,54,109. The matter is one of first impression and no authority directly in point has been brought to our notice by counsel for the parties.

The section of the Indian Income-tax Act directly in point is section 9 which lays down that "the tax shall be payable by an assessee under the head 'Property' in respect of the *bona fide* annual value of property consisting of any buildings or land appurtenant thereto of which he is the owner". Then certain allowances are mentioned which the assessee is entitled to deduct from the annual value of the property. The phrase 'annual value' is defined in sub-section (2) of section 9 which says that "for the purposes of this section, the expression 'annual value' shall be deemed to mean the sum for which the property might reasonably be expected to let from year to year". Reliance has been placed on behalf of the assessee upon section 3 (1) (b) of the Punjab Municipal Act, 1911, where the term 'annual value' is interpreted to mean "in the case of any house or building, the gross annual rent at which such house or building, together with its appurtenances * * * may reasonably be expected to let from year to year." Explanation (ii) of section 3 says "the term 'gross annual rent' shall not include any tax payable by the owner in respect of which the owner and tenant have agreed that it shall be paid by the tenant". But as pointed out by the Commissioner, there is no contention that any such agreement as is referred to here was ever entered into between the assessee and their tenants.

The question for decision is whether the house tax, which has been imposed by the Municipal Committee, Delhi, is included in the expression 'annual value', that is to say, whether the assessee is liable to pay an increased income-tax because the Municipal Committee has imposed the house tax upon him under the provisions of section 61 (1) (a) of the Municipal Act. The tax appears in reality and substance to be an occupation tax and is an incident of the property being occupied by the tenant. This is put beyond question by the rule, quoted by the Assistant Commissioner in his order, dated the 27th of July 1928, that, although for short periods the landlord may be liable to pay the tax even in the case of the premises lying vacant, yet if the house remains unoccupied for a period exceeding two months the owner can claim remission of the tax from the Municipal Committee. The mere fact that the landlord has to pay the tax to the Municipal Committee and that the tenant is left alone does not prove that it is not a tenant's tax. The reason is obvious. The landlord has got immovable property and is a person who has got a stake in it, while a tenant need not be a permanent resident of the locality and may be a mere bird of passage. The Legislature, therefore, in the interests of the Municipal Committee, has adopted the convenient method of realising the tax by making it demandable from the landlord, leaving the latter to realise it from the tenant. This mode of realisation, so eminently convenient to the Municipal Committee, cannot be made more onerous than it really is to the landlord, under the Income-tax Act. Judging

from the common sense point of view I fail to understand why this liability, which is imposed upon the landlord, to collect the tax from the tenant and to pay it into the coffers of the Municipality should be treated as forming part of the annual value of his property on which he should pay the income-tax. The question in my judgment, must be decided according to the provisions of the Income-tax Act and that Act does not contain anything which would support the contention of the Government Advocate.

I may here mention that the learned Government Advocate invited our attention to the case of *Veerabhadrah Iyer v. President, Corporation of Madras*(1). That was a case under Sec. 130 (1) of the Madras City Municipal Act, (III of 1904), and, if it is applicable at all, its reasoning tends to support the contention of the counsel for the assessee.

I would, therefore, answer the reference by holding that the house tax is not a part of the rent or the annual income accruing from the house property to the landlord, but is a mere liability of the landlord incidental to his owning the property which he lets out to the tenants on rent. It cannot, therefore, come within the meaning of the expression 'annual value' and, therefore, the assessee is not liable to an enhanced tax by the addition of the amount of the house tax to the annual rental of the property.

TEK CHAND, J.:—I agree in the answer to the reference given by my learned brother.

(305) IN THE COURT OF THE JUDICIAL COMMISSIONER, NAGPUR.

*Before Mr. Macnair, Officiating Judicial Commissioner and
Mr. Staples, Additional Judicial Commissioner.*

(18th April, 1929).

Moulana M. E. R. Malak

Assessee.

v.

The Commissioner of Income-tax, Central Provinces
and Berar .. Referring Officer.

Income-tax Act (XI of 1922), Secs. 2 (11) (b) and (10) (2)—Atba-e-Malak-Badar community—Assessment on basis of Abidi year—Two Abidi years determined as "previous year" by Central Board of Revenue—If legal—Sums paid to community members employed in shops—If deductible as salaries.

The assessees, the Atba-e-Malak Badar community, who made their accounts according to the Abidi year a lunar year 10 or 15 days shorter than a calendar year, were assessed for 1925-26 on the income of the Abidi year 34 terminating on 4-4-1924. For the year 1926-27 the assessee claimed to be assessed on the income of the Abidi year 36 (25-3-25 to 13-3-26), and contended that the income of the Abidi year 35 terminating on 25-3-25 should not be taken into account at all. On the refusal of the assessee to have the income of the two Abidi years 35 and 36, taxed jointly or separately, the Central Board of Revenue determined the period of the two Abidi years 35 and 36 as the "previous year" for the purpose of assessment for the year 1926-27.

(1) 35 Ind. Cas. 589.

HELD, that the determination of a period of 23 months as the previous year by the Central Board of Revenue was not unreasonable and did not contravene any of the provisions of Sec. 2 (11) (b) of the Income-tax Act.

The assessee further claimed a deduction in respect of sums paid to the members of the community employed in their shops. It was found that the community and not any individual member including the Head owned all the properties and that the members messed together but kept no accounts.

HELD, that the sums in question were not payments of salaries but disbursements to some of the owners and hence not deductible.

Case [Misc. Judicial Case No. 25 of 1928], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, Central Provinces and Berar, for the opinion of the Court.

CASE.

Moulana M. E. R. Malak of Nagpur, has, in an application under section 66 (2) of the Indian Income-tax Act, asked for the following points to be referred to the High Court:—

1. Whether in the circumstances of the present case, the Central Board of Revenue was competent, in exercise of the powers conferred by sub-clause (b) of clause (11) of section 2 of the Indian Income-tax Act, 1922, to determine the period of two Abidi years 35 and 36, (i.e., from 5th April 1924 to 13th March 1926), to be the previous year for the purpose of assessment for the year 1926-27.
2. In view of the fact that the Abidi year 35 ended on the 25th March 1925, was the assessee bound to state the income of that year in the return for the year 1926-27.
3. Whether the action of the Income-tax Officer in not allowing the assessee to tender evidence of the employees in proof of the fact of payment of salaries to them was legal.
4. Whether in view of the terms of the two trust deeds, dated 25-8-17 and 25-11-22 and the Reference order of the High Court, dated 4-8-27, in Income-tax Reference Case No. 5 of 1926, holding that the two trust deeds do not constitute a trust at all, the finding of the Assistant Commissioner of Income-tax that the members of the staff employed in the Mehdibagh shop are jointly the owners of the business and that the sums paid to them are only disbursements to owners and not payments of salaries is valid in law.
5. Whether the action of the Assistant Commissioner in disallowing the amount of salaries of the superior staff which is expenditure incidental to earn the assessable income, was legal.
6. In view of the fact that the assessee has already been taxed on Rs. 2,000, as interest accrued (though not realised), from Syed Mohammad Raza, during the assessment year 1925-26, was it legal on the part of the Income-tax Officer to tax him over again on Rs. 1,706, which was the interest actually received during the year 1926-27.

7. Was the Assistant Commissioner justified in disallowing loss of Rs. 424 and 641 on account of breakages of articles for sale on the ground that no stock account was maintained.
8. Is the expense on account of cart hire for carrying goods from one shop to another or for carrying aerated waters to the customers in the nature of direct charges so as to be disallowed.
9. Whether the action of the Income-tax Officer in adopting a higher percentage rate of profits than those of the other shops dealing in the same kind of merchandise was justified under law.

2. I beg to give below the facts of the case as regards each point and my opinion on it:—

Point 1. Facts.—Moulana M. E. R. Malak the spiritual head of the “Atba-e-Malak Badar Community” of Nagpur, has adopted for his “previous year” what he calls the “Abidi” year which corresponds with the first day of Ramzan and ends with the last day of the month of Shaban. Owing to its being a lunar year, it falls short by 10 or 15 days of the calendar year, every year. This Era seems to have started some 37 years ago, perhaps with the formation of this sect. Accounts were made according to this year and profits were assessed as:—

Profits of the Abidi year				Assessed for the year	
„	31	ending on	6-5-1921	„	1922-23
„	32	„	26-4-1922	„	1923-24
„	33	„	15-4-1923	„	1924-25
„	34	„	4-4-24	„	1925-26
„	35	„	25-3-1925	Income not returned nor assessed.	
„	36	„	13-3-1926	Income returned for assessment in the year 1926-27.	

It will thus appear that within one Financial year, i.e., the year ending on the 31st March 1925, two Abidi years, i.e., 34 and 35 had closed, i.e., the first on the 4th April 1924 and the second on the 25th March 1925. For assessment for 1925-26 the income of Abidi year 34 only was returned and assessed. For assessment for 1926-27 the income of the Abidi year 36 was returned. It was, during the course of this assessment, found that the income of Abidi year 35 had not been either returned or taxed and to assess the income of this year, a case under section 34 of the Income-tax Act was separately started. Objection was taken to this. The Income-tax Officer, Nagpur, then gave the assessee the option to have the income of two Abidi years 35 and 36 either taxed jointly or separately. As his two written replies, one dated the 7th January 1927 and the other not dated will show, he did not agree to the two years' income being taxed together; nor did he, except under protest, agree to the two years' income being taxed separately. It was then that the Central Board of Revenue in the exercise of the powers conferred by sub-clause (b), clause (11) of section 2 of the Indian Income-tax Act, determined the period of the two Abidi years 35 and 36 to be the “previous year” for purposes of assessment for the year 1926-27 (vide copy of Notification dated the 21st March 1927, Ex. C.). The case started under section 34 of the Income-tax Act was dropped and the income of the period from the 5th April 1924 to 13th March 1926 came to be assessed in one case.

Opinion.—These are the circumstances under which the notification in question was issued. It remains to be considered whether under these circumstances the Central Board of Revenue was competent to issue such a notification.

It is contended that the Central Board of Revenue had no power to determine the previous year as in the present case the accounts of each Abidi year were made up to a particular date within the financial year and each Abidi year was admitted to be the previous year for purposes of assessment of the assessee's income. Much reliance seems also to have been placed on the instructions contained in paragraph 5, page 78 of the Income-tax Manual wherein it is observed:— "This gave rise to difficulties in case of certain communities whose commercial year is not necessarily the calendar year but is a period which expressed in calendar months varies from year to year and in one year may be slightly over or in another slightly under 12 months." On the strength of this it is argued that as the period in question was neither slightly over nor slightly under 12 months, but consisted of 23 months and 10 days it could not be declared the "previous year." In the first place I beg to submit that the instructions as given in the Manual are simply for the use of the Department. They are not rules framed by the Central Board of Revenue under any section of law and cannot therefore have the force of law. In the second place the instructions in question are simply meant to distinguish between the definitions of "previous year" in the present Act and that in its predecessor, the Act of 1918. In the third place, sub-clause (b), clause (11) of section 2 which gives the power to the Central Board of Revenue to determine the previous year is quite independent of sub-clause (a) and does not contemplate of the period being slightly less or slightly over twelve months. To me it seems that it was quite within the competence of the Central Board of Revenue to issue the Notification in question. I submit this question be answered in the affirmative.

Point 2. Facts.—In November 1926 it was detected that the income of the Abidi year which ended on the 25th March 1925 had not been assessed and therefore a notice under section 34 of the Income-tax Act was issued. The result of this would have been a single assessment on the incomes of the Abidi years 34 and 35 as both of them ended within one financial year ending in March 1925. But the applicant refused to make a return of the income of the Abidi year 35 either separately or jointly with the income of the Abidi year 34 (vide his application dated the 3rd January 1927—Ex. D.). Thus he wanted that the income of the Abidi year should not be assessed at all, i.e., neither independently nor with the income of the year 34, though after the notification was issued, he began to take the plea that the income of the Abidi year 35 could be assessed for 1925-26 under section 34 (vide ground of appeal (d)—Ex. E). This plea was taken when the applicant thought that action under section 34 had become time barred. In fact, as stated above, it was originally proposed to do this and that was why case under section 34 was started. But as the applicant did not agree to it, it was dropped. Even till the issue of the notification under section 2 (11) (b), the assessee was given the option to have the two incomes, i.e., of the years 35 and 36 assessed separately or jointly; but he agreed to neither. The intention seems to have been not to pay tax on the income of the Abidi year 35 at all.

Opinion.—It was under the circumstances given above that the notification was issued and under the notification the applicant is bound to return the income of the Abidi year 35 for assessment for 1926-27. I submit this point be answered in the affirmative.

Point 3.—Facts.—A brief history of the assessee and his followers is already given in the statement of the case submitted to this Hon'ble Court under this office letter No. 18/18, dated the 28th September 1926, and its enclosures. For easy reference a mention of a few salient and relevant facts may be made here.

In the extract from the Phrenological Journal of October 1906, which was filed by the applicant himself, and in which he believes, it is stated; "The late Mr. Malak's plan was to form a society whose work should be to do good to the members, to their fellow-brethren and the persons who were likely to join the Society." Again in the history of their constitution as given by the applicant himself, the followers are classed as "Awaloons" (Ecclesiastics) who reside at Mehdibagh and "La-hequoons" (Ordinary members) who reside outside Mehdibagh and are owners of property. Those who reside at Mehdibagh have made over their property to the institution and have entered into certain pledges with the head of the Society. Some of the pledges are:—"(3) That we shall seek no personal advantage for ourselves." "(4) That we shall be content with such provisions for ourselves and our families as the said Moulana H. M. Malak Sahib or his deputy for the time being may make. We shall devote no part of our energies to acquire money or property for ourselves."

The object of the trust deed is said to be "for providing all the members of the Atba-e-Malak Badar Community with board, lodging, clothing and other necessities of life as I, and after me, the said Dayee, may deem fit." It was also stated in written arguments in the last reference case: "The trust deed aims at the feeding and clothing of the members of the community * * * *". Then in the extract from the Phrenological Journal referred to above, it is further stated:—"They are all fed, clothed from one place, they all dine in one place, the women behind a partition." In their judgment in the reference case dated the 4th August 1927, even the Hon'ble Judges of this High Court have held: "The property belongs to the Community and does not belong to any particular individual including the Trustee. The Dayee, in short, holds sway over the property only in his capacity of a spiritual head and has no personal interest therein * * * *". In the same judgment it is further observed: "Here we have in fact a small body of persons united by the bond of a common religion who have bound themselves into a society more or less of a communistic nature." All that is said above led to the conclusion that this communistic society lived, fed and clothed together with the exception perhaps of their head. Therefore enquiries were started to find out if the pays to Mahdibaghwalas serving in different shops were actually disbursed and whether or not they were fed and clothed together. On the 4th January 1926, Sheikh Tyeb, the agent of the applicant, was directly questioned on this point and he stated:—"No communal mess as such is maintained in connection with the business of Mr. M. E. R. Malak, but the members of the community, who are mostly employed in his business, have established a mess for their own use and at their own expense. The mess has got no concern, whatever with either Mr. M. E. R. Malak or his business as such. Members contribute about 50 per cent. of their salary towards the cost of their boarding in the mess, but almost every one of them has got some sort of separate arrangement for tea, light refreshment, etc., in his own house; just a few of them have got their own kitchens as well and are not members of the mess. The accounts of the mess are maintained separately by one of us, but there are only Kacha accounts which are destroyed after a few months. I cannot say at present without legal advice whether I should like to produce the mess accounts, but I think that as they have no connection with the business of Mr. M. E. R. Malak, the Income-tax Department cannot legally enforce their production. About 15 years before now when the business of the Malak Sahib was on a very limited scale, no salaries were paid to members of the community working in the shops but with the expansion of his business it was found more advisable to pay regular salaries for work done instead of supplying all the requirements of the staff as was done before, and since then salaries have been regularly paid. Small increments are also given. The supply of free board, clothing, etc., has since been stopped," and then on a later date said:—"I made enquiries

to-day and find that no mess accounts whatever are maintained. They were never maintained as we fully trusted the Manager for the time being. Credit purchases of stores—which are rare—are paid for in cash within a short time and there is no need to keep an account of them. I also looked into our shop accounts and did not find a credit of Rs. 5,000 withdrawn from Narayan Singh. The money was directly made over to the Manager of the mess for mess expenses. I do not know who was the Mess Manager then.” The evasive statement and its partial withdrawal later on suggests how far it can be believed. The statement: “The supply of free board, clothing, etc., has since been stopped”, does not find its support either in the trust deed of 1922 wherein it is reiterated that the object of the trust shall continue to be “For providing the members of the Atba-e-Malak Badar Community with board and lodging, clothing and such other necessities of life as I may deem fit,” or in written arguments or other documents filed by applicant in last reference case. The fact is that the “Awaloons” who live at Mehdibagh are given free quarters, free boarding, free clothing and other necessities of life.

I shall now show how the expenses under the head “Staff” have increased. As stated above, it is admitted that no payment was made to the staff up till 1919. The Act of 1918 required a return of the income to be made and it was from this year that accounts came to be called and examined and assessments were based on them. The assessments for the years 1919-20, 1920-21 and 1921-22 were compounded under the provisions of that Act and no figures of the payment to the staff are available or were furnished. The first return for the Abidi year 31 came to be made for assessment in 1922-23 under the Act of 1922. The pays of only the superior staff (which means the Mehdibaghwalas) showed great rises as:—

Name		Abidi year		
		30	31	
Sheikh Arif	...	Rs. 80	160	} Pays tried to be kept below Rs. 2,000 a year.
Sheikh Tyeb	...	" 60	150	
" Saleh	...	" 65	150	
" Shamsheer	...	" 65	150	
" Saleh Hassankhan	...	" 55	125	

Name		Abidi year		
		29	30	
Sheikh Ysuf Bhai	...	Rs. 35	100	
Mulla Jaffar	...	" 55	100	
Ibrahim Riza Saheb	...	" 35	125	
Mulla Sufi	...	" 35	75	
" Yahya Bhai	...	" 35	100	
Bhai Mohammad Bhai	...	" 30	75	

This shows that as the scrutiny of accounts in the assessment cases became stricter and stricter, not only were pays claimed, but there was *per saltum* rise in them, the rise in certain cases being more than 180 per cent. The pays as claimed, had been allowed up till 1925-26 as the real history of the institution was not fully disclosed. In this year in the reference case last sent up to this Hon'ble Court, the facts described above came to light and thereafter the question of allowing the pays as a deduction came to be considered and documentary evidence was insisted upon to find out whether the pays of the staff were actually disbursed as under the trust deed the Awaloons were entitled to be fed, clothed and supplied all necessities of life by the institution.

On the 30th April 1927, when the return for the two Abidi years was filed under protest in the prescribed form, the following incomes were shown:—

			Rs.	A.	P.
Business	...	...	21,557	1	5
Interest on securities	...	...	600	0	0
Property	...	...	8,165	8	0
Dividends	...	...	290	0	0
Ground-rent	...	...	400	0	0
Miscellaneous	...	...	25	0	0
Total			31,037	9	5

There was no disagreement as regards the income shown above excepting the one derived from business. In the two Abidi years the total sales amounted to Rs. 6,88,358 and Rs. 6,15,624 respectively; but the net income returned from them was Rs. 15,794-9-0 and Rs. 5,762-8-5, i.e., 2·3 and ·93 per cent. respectively. These small percentages of profit are due mainly to the adoption of small flat rates for calculating the profits and returning low incomes, and to a claim of a set off against it for high pays of the superior staff which claim absorbs practically the whole of the income. Lists of servants on all shops show 127 hands, of whom 34 are Mehdibaghwalas or superior staff and who, out of the total expenditure of Rs. 52,505 and Rs. 55,384 on staff, consumed Rs. 39,840 and Rs. 40,680 in the two Abidi years.

It was under the circumstances mentioned above, that the Income-tax Officer insisted upon a strict proof of the payment of the salaries to the superior staff and asked for documentary evidence including the production of the Kothar Mubarik account. The payments to the staff are recorded only in the shop daily cash book at the end of each month. There is no ledger for these payees. The shop account books do not show the receipt or the issue of the money from or to the Kothar Mubarik, i.e., the central account or the Malak's account. There is some account kept at Mehdibagh for the Malak and it is called the Kothar Mubarik account which was produced before the Income-tax Officer in 1921. This account book is now not produced on the pretext of its having been since discontinued. Moneys are sent to and received from Bombay and Umrer and references to this Kothar Mubarik account are even now made in the account books of Umrer and Bombay and still the Kothar Mubarik book is not produced. It is said that the Malak keeps no written accounts of the money that goes to him or is sent out by him; but this seems quite strange. When a man claims to be the Trustee and does business in a Bohra fashion and has got over 100 men to help him in the maintenance of accounts, it is not likely that such a book, the existence of which was once admitted, would be discontinued. As this book, from which only the accuracy of the accounts could be judged and which alone could prove that the superior staff had been actually fed by the institution or not, was not produced, the Income-tax Officer thought it was no use calling the staff (Mehdibaghwalas) and recording their statement, as it was but natural that they would state they got the pays. As the members of the superior staff were not called by the Income-tax Officer, this question came to be framed.

Opinion.—I am of opinion that the Income-tax Officer should have allowed the applicant to examine the superior staff though he could have drawn his own conclusions even after that. I beg to submit that as even after examining the superior staff, the Income-tax Officer would have come to the same conclusion as

he has done, the merits of the case are not affected by not examining these persons and as such this question does not affect the merits of the case at all.

Point 4. Facts.—In the appeal before the Assistant Commissioner, objection was taken to the disallowance of expenditure over the superior staff of servants and the Assistant Commissioner has considered the question from one more point of view which is:—“Are the members of the superior staff really servants of the shop, or do they form association of individuals participating in the prosperity of the concern. If the former, the salaries would certainly be allowable. If the latter, they are not entitled to deduct this expenditure from the taxable income,” (vide para. 14 of Ex. G). And after referring to the trust deed, the transfer deed of the 9th June 1894, which is the first of its kind and which was executed by the principal members of the society including the late Malak and after taking into consideration the remarks of the Hon'ble Judges of this High Court quoted above, he has come to the conclusion that all the members of the Mehdibagh “therefore jointly are the owners of the business and sums paid to them are only disbursements to the owners and in no sense could these payments be called their salaries.”

The terms of the two trust deeds so far as they relate to this point have already been quoted above and so also the passages from the Judgment of this Hon'ble Court, dated the 4th August 1927, all of which have a direct bearing on this point. In the judgment referred to, it has been held: “The property belongs to the community and does not belong to any particular individual including the Trustee. The Dayee, in short, holds sway over the property only in his capacity as a spiritual head and has no personal interest therein * * *.” Thus there is no denying the fact that the property belongs to the community. It is contended that in the Judgment mentioned above, the Hon'ble Judges have held that the two trust deeds do not constitute a trust at all. But it is nowhere expressly said so in the Judgment. Even if it were, it would only mean that the property which is gifted to the community belongs to it. On the other hand what the High Court have held is: “There was no Wakf or trust of the property wholly for religious or charitable purposes and we are further of opinion that the property is not held in part for such purposes.” The several gift deeds that have been filed by the assessee also lead to the same conclusion, i.e., that the property is gifted to the community and is to be managed by the Malak for the benefit of the community only. There is thus no doubt in believing that the property belongs to the community, the spiritual head being its manager only.

According to the distribution of assesment work at Nagpur, an Additional Income-tax Officer deals with salaried assesseees (whose principal source of income is salary). Other cases are taken up by the Income-tax Officer himself. Four of the members of the superior staff of the applicant have therefore been taxed for 1927-28 by this Additional Income-tax Officer separately as returns under section 21 were received by him. He passed these orders without waiting for the original case to be disposed of by the Income-tax Officer, and the members of the staff suffered to be so taxed. As assesment against them were unjustifiable they have been cancelled by me.

Opinion.—I am therefore of opinion that the Assistant Commissioner of Income-tax was quite correct in his finding that the members of the staff employed in the Mehdibagh shop are jointly the owners of the business and that sums paid to them are only disbursements to the owners and not salaries; and I am further of opinion that such a finding is valid in law.

Point 5. Facts.—The facts concerning this point have been somewhat sufficiently given above and I need not repeat them here.

Opinion.—In the circumstances of the case detailed above, I am of opinion that the action of the Assistant Commissioner in disallowing the amount of the salaries to the superior staff was quite legal and I would submit that this question also be answered in the affirmative.

Point 6.—Facts.—Syed Mohammad Raza and others of Nagpur had borrowed a loan of Rs. 12,000 from the applicant's predecessor and executed a usufructuary mortgage deed dated the 4th November 1920. There was a correction deed also executed on the 25th August 1921. The rate of interest was 18 per cent. per annum and in case of default 24 per cent. per annum. The condition was that the profits of the mortgaged property (8 annas share of Gorewara and 8 annas share of Sonekham) be first credited towards interest and the remainder towards principal of Rs. 2,000 annually. Thus the debt was to be liquidated in six years' time. The applicant did not make up the accounts of the debtor annually; but had been sending him certain accounts and telling him how his account stood. During assessment proceedings for 1925-26 when the realisations from interest from this debtor were denied by the applicant's agent, the debtor was called to produce the accounts which the applicant had sent him, and he filed them. That case came up in appeal to me as Commissioner and in my order dated the 5th July 1926, I have written as:—"As regards Syed Mohammad Raza the accounts have not been produced and it is said that the accounts have not been made and that the money as received is credited towards the accounts and that the accounts will be settled after the whole amount is paid up. I asked the appellant and his counsel, whether it was not the practice of the appellant to appropriate the payments first towards the interest and then towards capital. No direct reply was given to me. Mr. Wazzalwar, after all said: 'At the time of the final accounts we would appropriate the payments first towards interest and then towards the principal.' Thus it became apparent why those accounts were not finally settled. If payments had been made in any year money would be first credited towards interest. This is also clear from the statement which Syed Mohammad Raza has filed in this case. This statement of account, as sent by Sheikh Tyeb, agent of the appellant to his debtor, shows that at the end of the year out of the income made about Rs. 2,000 used to be added as due to interest and as the accounts were kept in the mercantile fashion, Rs. 2,000 a year until the whole amount is paid up could be taken as income from interest on the mortgage bond." In his letter dated the 23rd March 1928, Sheikh Tyeb, the agent to the applicant shows that the realisations after deducting the expenses are:—

Periods.	Amount realised.		
	Rs.	A.	P.
During the year ending 31-3-21	255	6	3
" " 31-3-22	1,642	12	3
" " 31-3-23	1,969	13	6
" " 31-3-24	1,327	10	9
" " 31-3-25	8,462	1	9
" " 31-3-26	46	7	0
	<hr/>		
Total	13,704	3	6
	<hr/>		

According to the conditions of the mortgage deeds (copies of which are recently filed), as described above, these annual realisations should have been appro-

priated first towards interest on the principal amount outstanding and then the balance towards Rs. 2,000 of the principal. The contention of the applicant was that of Rs. 13,704-3-6 collected up to the end of March 1926, only Rs. 1,704 should have been taxed for 1926-27 and as Rs. 2,000 have already been assessed for the year 1925-26, this amount of Rs. 1,704 should not be taxed.

Opinion.—In the first place it appears to me as if the question is not framed very correctly. The words “Though not realised” as used in this question seem to imply that no money on account of interest had been received: which is not correct. The list of realisations, as given above, shows that as much as Rs. 5,195-10-9 had already been realised by the 31st March 1924 and under the conditions of the mortgage deeds, all this was interest and should have been taxed then. But only Rs. 2,000 came to be taxed as the accounts were not then produced. Nor is it a fact that the Income-tax Officer has taxed over again the sum of Rs. 1,704 “which was the interest actually received during the year 1926-27”. According to the accounts furnished by the applicant he only received Rs. 46-7-0 in 1925-26; but in this and the preceding year for both of which the assessment is made he has actually received Rs. 8,508-8-9 and if the interest on the principal of the two years together with the arrears of interest of the previous year were calculated, the whole of this amount of Rs. 8,508 would be interest and should have been taxed in the assessment under reference; but in the hurry to finish up the case and owing to the non-production of the accounts before him, the Income-tax Officer forgot to tax the whole of it and taxed only Rs. 1,704, for which mistake of the Officer the applicant should be grateful. For reasons given above, I would submit that this question be answered in the affirmative.

Point 7. Facts.—For the breakages of wares Rs. 424 were claimed as expenses for the Abidi year 35 and Rs. 641 for the Abidi year 36. The Income-tax Officer did not allow this as expenses because no account of the stock purchased and sold or broken was kept in entirety; and on the same ground the Assistant Commissioner disallowed the claim.

Opinion.—To me this appears to be a loss of stock in trade and I have allowed this under the powers given to me under section 33. This point therefore is not referred for the decision of the Hon’ble Judges of this Court.

Point 8. Facts.—The applicant seems to be keeping carts for sending out goods from shop to shop and for distributing soda. He had on this account claimed Rs. 1,269-3-0, as expenses during the Abidi 35 and Rs. 793 plus Rs. 610, total Rs. 1,403 for the Abidi year 36. These were disallowed by the Income-tax Officer and the Assistant Commissioner on the ground that they were direct charges. As these appear to be indirect charges I have, in my powers under section 33, allowed the applicant these expenses. Therefore this question too now does not arise and is not referred to the High Court.

Point 9. Facts.—The applicant does not keep closed accounts, that is to say, he does not take stock at the end of the year. He calculates his profits at flat rates called “the percentages.” To find out the correct percentages the Income-tax Officer made enquiries of the purchase and sale prices of the applicant. The applicant has his own men at Bombay who purchase articles of merchandise and send them to Nagpur. They prepare their own Bijaks (Invoices) and send them here. The Income-tax Officer asked for the original Bijaks of the actual sellers which were not produced. From the enquiries which he made of the purchase and sale prices of articles at this shop, he calculated the margin of profits that this applicant was making. He, however, observed that

from the general enquiries made from the other shop-keepers and from the applicant's own list, the applicant was found to charge profits higher than any other shop-keeper and to this end he quoted certain examples also, viz his order dated the 30th September 1927, copy of which is enclosed (Ex. F). He then went on to say:—"I have therefore determined the following percentages for the Abidi year 35 and will calculate the profits accordingly:—

Sale.			Percentage adopted by the assessee.	Profit as per assessee.	Percentage adopted by the Department.	Profit as per Department.
Itwari	...	1,88,662				
Sadar Branch	...	2,20,223				
Sitabuldi	...	80,435				
		4,89,320	12½	61,165	13	73,395
Cloth sales at Itwari	...	15,212	10	1,521	12½	1,901
Medicine sales at Itwari	...	50,147	12½	6,268/ 6	15	7,521
Sales of Umbrella at Itwari.		30,850	3	925/ 8	5	945
Sales of Manihari at Umrer.		21,157	10	2,115/11	10	2,115/11
Sales of Kerosine Oil at Umrer	...	18,904	2	378	5	945
Sales in Chhindwara shop provisions	...	14,527	10	1,452/11	10	1,452/11
Soda factory at Sadar	...	18,147	20	3,629/ 6	25	4,537
Sales of Kirana at Itwari	...	30,094	6½	1,880/10	6½	1,857
		6,88,358		79,336/ 4		95,266/ 9

Thus in the order of assessment passed by the Income-tax Officer there is no mention whatever that the percentages at which he has calculated the income of the applicant are in any case higher than those of other shop-keepers dealing in the same kind of merchandise at Nagpur. In order to strengthen his calculations of percentages he has undoubtedly cited examples of sale prices to show that this applicant has been charging more profits than other traders dealing in the same kind of merchandise. But it is nowhere said in the order of assessment that these percentages are higher than those adopted in the case of other merchants.

Opinion.—This question, therefore, does not arise out of the facts of the case and could not be asked to be referred under section 66 (2) and is therefore not referred to the High Court. I may add that it is the common knowledge of all that all traders do not charge the same percentages of profit. These percentages vary with traders, with facilities given by the shop, with the situa-

tion of the shop, with the kind of customers patronizing them, with the prestige and status of the shop and so many other factors; and depend upon the trade conditions which vary from year to year. Even if, therefore, the Income-tax Officer had adopted higher percentages in the applicant's case, there was nothing against law in it. In fact, it is totally a question of fact as to what percentages should the Income-tax Officer adopt for finding out the income of any particular assessee and no reference can be asked to be made about it *Dagaram Sobharam v. Commissioner of Income-tax, Punjab* (1). On this ground too the question cannot be referred to the High Court.

3. In conclusion, I would submit that the application fails on all the points referred to this Hon'ble Court and be rejected.

H. S. Gour, M. B. Niyogi and A. V. Wazalwar, for the Assessee.

D. N. Chaudhari, for the Crown.

JUDGMENT.

This is a reference under section 66 (2) of the Indian Income-tax Act, XI of 1922. The first two points which have been referred to this Court for decision by the Commissioner of Income-tax are stated in the following terms:— (1) Whether in the circumstances of the present case, the Central Board of Revenue was competent, in exercise of the powers conferred by sub-clause (b) of clause (11) of section 2 of the Indian Income-tax Act, 1922, to determine the period of two Abidi years 35 and 36, (i.e., from 5th April 1924 to 13th March 1926) to be the previous year for the purpose of assessment for the year 1926-27. (2) In view of the fact that the Abidi year 35 ended on the 25th March 1925, was the assessee bound to state the income of that year in the return for the year 1926-27.

2. The *Atba-e-Malak Badar Community* of Nagpur has for a number of years made up accounts according to the Abidi year which commences with the first day of Ramzan and ends with the last day of the month of Shaban. This year is a lunar year and is always 10 or 15 days shorter than a calendar year. Under section 3 of the Income-tax Act income-tax for any year is charged in respect of all income, profits and gains of the previous year. Section 2 (11) defines a "previous year". Under section 2 (11) (a) the assessee has an option to take the year ending on the day on which the accounts have been made up as the previous year; but it is clear that he has not the option to take a period which is not a calendar year as the previous year. Section 2 (11) (b) states that such period as may be determined by the Central Board of Revenue, or by such authority as the Board may authorise in this behalf, may be considered the previous year. For a number of years the profits have been assessed with reference to the Abidi year. The authority authorized by the Board, i.e., the Commissioner of Income-tax in this Province, has, under section 2 (11) (b), taken the Abidi year as the previous year.

3. Now the Abidi year No. 34, terminated on 4-4-24 and income-tax for the year 1925-26 was assessed on the profits for this year. Abidi year No. 35 terminated on 25-3-25, a few days before the year 1924-25 expired. The Community when making a return for assessment in the year 1926-27 showed the income for the Abidi year No. 36, i.e., for the period 25-3-25 to 13-3-26. The assessee took the position that the income during the Abidi year No. 35 should not be taken into account at all. The Income-tax Officer, Nagpur, gave the

assessee the option of having the income of the two Abidi years 35 and 36 taxed jointly or separately. The assessee would not agree to the very reasonable proposition that he should pay income-tax on each year's income separately. The Central Board of Revenue then determined the period of the two Abidi years 35 and 36 as the previous year for the purpose of assessment for the year 1926-27.

4. It is urged on behalf of the assessee that the powers given to the Central Board of Revenue by section 2 (11) (b) of the Act do not permit the determination of a period of over 23 months as the previous year. There is nothing in section 2 (11) (b) which expressly prevents such determination. The rule under the Act, which delegates the authority to the Central Board of Revenue for determination of a previous year, allows the Commissioner of Income-tax to determine as the previous year, a period between 11 and 13 calendar months and this indicates that the Central Board of Revenue can fix a period less than 11 or more than 13 calendar months. It is urged on behalf of the assessee that he long ago exercised an option given him by section 2 (11) (a) and chose as his previous year the Abidi year: the Income-tax authorities having accepted the exercise of his option must continue to take an Abidi year as the previous year. But, in the first place, section 2 (11) (a) does not give the assessee an option to take a period not a calendar year as the previous year and in the next place there is nothing in section 2 (11) (a) which makes it necessary for the Income-tax authorities to take the Abidi years as the previous year in subsequent years because they have done so in a particular year.

5. It is next urged for the assessee that the Central Board of Revenue must make their determination in a reasonable manner and that it is unreasonable to fix a period of approximately two years as the previous year. It is sufficient to say that we do not find the action of the Central Board of Revenue unreasonable in the peculiar circumstances which we are considering: the assessee for one year returned the accounts upto 4-4-24; for the next year he returned the account of the period 25-3-25 to 13-3-26. It is admitted before us that he should have made a return for the profits of the intervening year. For a number of years he has been taxed with reference to profits for periods of about 11½ months. It is quite possible that in some years he has been taxed at a lower rate than if he had been taxed on profits for full 12 months. It appears equitable that he should now be taxed on profits from 4-4-24, the date which he himself chose as the date up to which accounts should be furnished for assessment for 1925-26 to 13-3-26, the date upto which according to him accounts should be returned for assessment in the year 1926-27. We consider that the determination by the Board of Revenue did not contravene any provisions of section 2 (11) (b) of the Act and was not unreasonable. We have, then, no power to interfere with this determination. We answer the first point in the affirmative. In view of the determination of the Central Board of Revenue, the second point must also be answered in the affirmative.

6. We next consider point No. 4 which is stated as follows:—“(4) Whether in view of the terms of the two trust deeds dated 25-8-17 and 25-11-12 and the Reference order of the High Court, dated 4-8-27, in Income-tax Reference Case No. 5 of 1926, holding that the two trust deeds do not constitute a trust at all, the finding of the Assistant Commissioner of Income-tax that the members of the staff employed in the shop are jointly the owners of the business and that the sums paid to them are only disbursements to owners and not payments of salaries is valid in law.” Section 3 of the Income-tax Act authorises taxation on the profits of an association of individuals. The statements of the agent of the applicant quoted by the Commissioner of Income-tax in his statement of the

case show that the members of the community mess together and no mess accounts whatever are maintained. In an opinion of this Court on a Reference* made on a previous year by the Commissioner of Income-tax with respect to the income of this community it was held:—"The property belongs to the community and does not belong to any particular individual including the trustee." The members of the staff employed in the Mehdibagh shop are members of the association of individuals, who are the owners of the property and whose expenses are met from the profit of this property without any account being kept. It is clear, then, that on the assumption that certain sums are made over to them as monthly payments, these sums come from the joint property and remain joint property in the possession of some of the joint owners. If sums are made over to them, they are not payments of salaries but disbursements to some of the owners. We answer point No. 4 in the affirmative.

7. Point No. 3 is as follows:—"Whether the action of the Income-tax Officer in not allowing the assessee to tender evidence of the employees in proof of the fact of payment of salaries to them was legal." We hold that it was unnecessary to take evidence on the point whether sums were handed over to particular members of the community each month.

8. In consequence of our decision on point No. 4, No. 5 which is as follows:—"Whether the action of the Assistant Commissioner in disallowing the amount of salaries of the superior staff which is expenditure incidental to earn the assessable income, was legal" must be answered in the affirmative.

9. The remaining point referred is No. 6:—"In view of the fact that the assessee has already been taxed on Rs. 2,000 as interest accrued (though not realised) from Syed Mohammad Raza during the assessment year 1925-26, was it legal on the part of the Income-tax Officer to tax him over again on Rs. 1,706 which was the interest actually received during the year 1926-27." As the Commissioner of Income-tax has pointed out, the question to be decided is not accurately stated. In the period to which the account relates the assessee received over Rs. 8,000 towards the principal and interest on a loan of Rs. 12,000. The interest which has accrued on this loan since it was made up to 13-3-26 amounts to Rs. 10,000 or so. Because the applicant has previously been taxed on Rs. 2,000 out of Rs. 10,000 interest due there is no reason why he should not now be taxed on a portion of the Rs. 8,000 received during this year. As the Commissioner of Income-tax points out, a considerable portion of the receipt has escaped taxation. The Income-tax Officer was wrong in treating the amount received upto 31-1-26 as repayment of the whole capital and Rs. 1,704-3-6 as interest. Much more than Rs. 1,704-3-6 plus Rs. 2,000 has been received as interest and there is nothing inequitable in assessing the applicant to Rs. 1,704-3-6 this year after assessing him to Rs. 2,000 for the previous year.

10. The costs will be borne by the applicant Moulana M. E. R. Malak. We fix Rs. 200 as counsel's fee.

* Reported as *M. E. R. Malak v. Commissioner of Income-tax* 2 I. T. C. 443.

(306) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Mr. Justice Wallace, Mr. Justice Beasley and Mr. Justice Madhavan Nair.

(25th April, 1929.)

A. M. K. Muthukaruppan Chettiar and another

Assessees,

v.

The Commissioner of Income-tax, Madras.

Income-tax Act (XI of 1922), Secs. 4 (2) and 66 (3)—Money-lending business—Remittance from foreign branch to British Indian branch—Sums entered in accounts as loans and interest credited—Assessment as remittance of profits—Question if one of law for reference.

The assessee carrying on money-lending business remitted in the account year sums aggregating to two lakhs from their Penang shop to their Rangoon shop for providing the latter with funds to pay off its creditors. Of the remitted sums one lakh was credited in Rangoon accounts in favour of Penang branch and was retained and utilised in the business. The other lakh credited in favour of Head Quarters, was returned in the succeeding year to Penang. The remittances were exhibited in the accounts as loans, interest charged and adjusted in the accounts.

On an assessment of this latter sum of one lakh under Sec. 4 (2) of the Income-tax Act the assessee's contention that the remittance was a loan in the usual course of business repaid in the succeeding year was overruled.

On an application under Sec. 66 (3) of the Income-tax Act for a reference, the High Court refused to call on the Commissioner to state a case.

Application [O. P. No. 285 of 1928], under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922), for an order to direct the Commissioner of Income-tax, Madras, to state a case for the opinion of the High Court.

ORDER OF COMMISSIONER UNDER SEC. 66 (2).

This is an application under section 66 (2) of the Income-tax Act.

2. The petitioners—A. M. K. Muthukaruppan Chettiar and Karuppan Chettiar—are members of a Hindu undivided family residing at Karaikudi within the jurisdiction of the Income-tax Officer, Karaikudi First Circle. They carry on the business of bankers and money-lenders in and outside British India.

3. They are the proprietors of two banking concerns one at Rangoon and the other at Penang. The businesses in those places are managed by agents appointed by them holding their power of attorney.

4. Most of their capital is employed in their business at Penang. Thus out of a total sum of \$15 lakhs employed in that business—as reflected in their balance sheet as on 30th Panguni Krodhana (12-4-26)—about \$12.8 lakhs represents their own money, i.e., their capital supplemented by the large profits which they have earned in that business; and only a sum of \$2.2 lakhs represents capital borrowed from others. Of the total funds employed in that business about \$5 lakhs are invested in immovable properties, the balance being debts due from sundry debtors and investments in their Rangoon shop.

5. The business at Rangoon is on the other hand carried on entirely with the aid of capital borrowed from others. (The petitioners have, it is true, a nominal capital of Rs. 48,000 but this is not even sufficient to meet the excess of the interest payments over the interest receipts). Such borrowed capital amounts approximately to Rs. 12½ lakhs. The petitioners have however withdrawn from this business Rs. 6.4 lakhs. A sum of 4 lakhs out of the money withdrawn was invested in the purchase of rice mills and properties and it is admitted that most of this has been lost. A further sum of Rs. 1.6 lakhs has been invested in a partnership in British India and Rs. 20,000 has been expended on the renovation of a temple.

6. The petitioners having practically no capital of their own in the Rangoon business and they having in addition drawn heavily on the resources of that business, that business was not in a position to repay its numerous creditors. The petitioners therefore provided the Rangoon business with funds by instructing their agent at Penang to remit money to Rangoon. The sums so remitted were debited in the Penang accounts to a folio headed "Rangoon business". During the year of account Krodhana—13th April 1925 to 12th April 1926,—the Rangoon shop received from the Penang agent a sum of Rs. 2,00,000 on three occasions—two instalments of Rs. 50,000, each and a third instalment of one lakh. The Rangoon agent credited the first two amounts in the Rangoon accounts in favour of the Penang business. This amount was later on exhibited in the Rangoon accounts by means of certain fictitious entries, as having been returned to Penang; but actually, as the petitioners themselves now admit, it was retained and utilised by them at Rangoon. The other sum of 1 lakh was credited in the Rangoon accounts, not in favour of the Penang business, but in favour of "oor"—i.e., the petitioners themselves. It may be taken that this sum which continued to be employed in the Rangoon business for a period of six months was in the succeeding year returned, in effect to Penang—for, though it was not actually remitted back to Penang it was handed over at the instance of the Penang agent to a third party in India who wanted to withdraw money from a business of his at Ipoh and who for that purpose had an equivalent amount paid out of his Ipoh business to the petitioners' Penang business.

7. In the assessment of the year 1926-27 which was made under section 23 (4) of the Income-tax Act the Income-tax Officer adopted the sum of Rs. 1,00,000 first referred to above as the profits of the Penang business received in British India and the petitioners acquiesced in the assessment. He subsequently formed the opinion that the other sum of Rs. 1,00,000 received from Penang at Rangoon should also have been taxed. He therefore took action under section 34 and called on the petitioners to show cause why that sum should not be treated as the profits of the Penang business received in British India and assessed under section 4 (2).

8. The petitioners objected to the proposal on the ground that the remittance from Penang should be presumed to be the capital of that business and contended *inter alia*:—(1) that the remittance from Penang to Rangoon was made in the usual course of business, and (2) that the transaction merely represented a loan by the Penang business to the Rangoon business which was re-paid during the succeeding year. It was mentioned by way of argument in support of the latter position that interest would be charged and adjusted between the Penang and Rangoon businesses in respect of that loan.

9. On an examination of the accounts and evidence produced by them, the Income-tax Officer found: (a) that the remittance made from Penang to Rangoon was for the purpose of restoring the finances of the Rangoon business

which had been crippled by large drawings for investments and personal expenditure, (b) that a large portion of the funds of the Penang business consisted of profits that had accrued to the petitioners in that business and that the remittance was therefore a remittance of profits, (c) that no reliance could be placed on the ostensible nature of the entries in the Penang accounts, because, firstly, the petitioners had by means of false entries exhibited the first lakh of rupees which, admittedly, they had retained and utilised in India as having been returned to Penang, and, secondly, the amount of one lakh now in question was retained in the *Rangoon* accounts in favour of the petitioners themselves—“QOR”, (d) that the petitioners being the sole proprietors of both the businesses the mere fact that the remittance was exhibited in the accounts as a loan made by one business to the other did not prove that profits were not remitted to British India, (e) that the fact that interest was charged and adjusted in the accounts was not of importance as the adjustment was really only part of their method of calculating interest due to the proprietors on moneys left in the business and the transaction only amounted, in effect, to the petitioners paying interest to themselves and receiving it themselves, and (f) that the circumstances were such that the petitioners were merely drawing on their profits at Penang, the exhibition in the accounts of the sums remitted as a loan from one business to the other being merely a mask to cover the actual facts.

In view of the fact that the petitioners had not rebutted the ordinary presumption in law that such remittance represents profits and proved that the whole or any portion of the remittance in question was attributable to capital, and in view of the conclusion that he had arrived at from the state of the accounts, the Income-tax Officer taxed the petitioners on the sum of Rs. 1,00,000 in an additional assessment made for the year 1926-27.

9. The petitioners appealed against this assessment to the Assistant Commissioner but without success.

10. They now require me to state a case and refer for the opinion of the High Court the following question which is said to be one of law:—

“When two money-lending businesses are owned by the same individual one outside British India and the other inside British India and moneys are transferred temporarily from the former to the latter either for the purpose of earning more profits or as a loan bearing interest for exigencies of trade demand and the amounts so transferred are re-transferred to the sending firm within a short period during the year of account itself and interest upon such amount is received by the sending firm, whether the transfers of money are transfers of profits so as to amount to foreign profits received or brought into British India”.

11. The question contains important mis-statements of fact. Out of the sum of Rs. 2 lakhs received in Rangoon one lakh was retained and utilised in British India and was not sent back at all; while the other lakh of rupees was sent back, not during the year of account but in the succeeding year. Further, the interest credited to the “Penang shop” in the year of account (in respect of the earlier remittance of one lakh) was not sent to Penang but was only transferred to the petitioners’ personal account; while in respect of the other sum of one lakh no interest was adjusted either in the year of account or in the next year. Interest seems to have been adjusted in the year following, i.e., in the year Prabava but it does not appear to have been anything more than a book entry. The question propounded does not therefore arise on the facts of the case. The real question at issue is whether it was rightly found as a fact that the sums in dispute were drawn from the Penang profits.

12. On the merits, I consider that the amount of 2 lakhs was rightly taxed. Section 4 (2) of the Income-tax Act enacts "profits and gains of a business accruing or arising without British India to a person resident in British India shall, if they are received in or brought into British India be deemed to have accrued or arisen in British India and to be profits and gains of the year in which they are so received or brought.....". The petitioners admit that large profits accrued or arose to them in their business at Penang and that the remittances made to British India came out of the funds of their Penang business which consist of both capital and profits. The Madras High Court has repeatedly held that in such circumstances there is a *prima facie* presumption that the remittances represent profits unless the assessee proves the contrary. In this case the petitioners have not proved that the remittance or any portion thereof was attributable to capital.

The Income-tax Officer had on the contrary ample materials before him to justify his conclusion that the profits of the Penang business were remitted to British India. In the first place there were large withdrawals by the petitioners from their Rangoon business which is run purely on borrowed capital. Most of their moneys are in their business at Penang and in order to make good the withdrawals and place their Rangoon business in a solvent state they drew on their funds at Penang (which included a large amount of profits earned there). In my opinion it was right to infer from these facts that the money remitted to Rangoon had come out of the profits of the Penang business. It may be added that out of the total funds of about \$15 lakhs employed in the Penang business only a sum of \$2 lakhs represents capital borrowed. The petitioners are unable to prove that any portion of the borrowed capital was remitted to British India.

The assessment in this case rests entirely on findings of fact and I am of opinion that no question of law arises for decision. The application is therefore dismissed.

S. Srinivasa Ayyangar and S. Parthasarathy, for the Assesseees.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

1. That this petition do stand dismissed out of this Court; and

2. That the petitioners herein do pay to the Commissioner of Income-tax, Madras a sum of Rupees One hundred—(Rs. 100/-) only as and for his costs of this petition.

(307) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Sir Murray Coutts Trotter, Kt., Chief Justice, Mr. Justice Odgers and Mr. Justice Beasley.

(1st May, 1929).

The Pondicherry Railway Company, Ltd.

.. Assesseees.

v.

The Commissioner of Income-tax, Madras

.. Referring Officer.

Income-tax Act, (XI of 1922), Secs. 2 (4) and 10 (2) — Pondicherry Railway Company—Company registered in England—Concession from French

Government for constructing line—Agreement with South Indian Railway for constructing and working the line—Revenue collected, accounts kept and profits determined in British India—Company, if carrying on assessable business in British India—Portion of net profits payable to the French Government under concession—If deductible.

The Pondicherry Railway Company, Ltd., incorporated in England with its registered office, Secretary and Board of Directors in London, constructed a railway line under a concession from the French Colonial Government in consideration inter alia of making over to the latter one half of the net annual profits derived from working the line. The Company entered into an agreement with the South Indian Railway Company, whereby the latter undertook to work, manage and maintain the railway line with their own staff, rolling stock, plant, etc., as an integral part of their (South Indian Railway's) undertaking, and to pay over to the Company in India every six months in rupees the profits of the line arrived at in a certain manner. The gross receipts from the line were from time to time paid into Government treasuries in British India and treated as part of the South Indian Railway Company's income and a large part of the income was collected by the issue of through tickets and way-bills in British India by the officials of the South Indian Railway Company. The office of the Pondicherry Company was in the same building as the South Indian Railway Company's in London, the Secretary and two of the Directors of the South Indian Railway Company were the Secretary and Directors of the Pondicherry Railway Company.

The Agent of the South Indian Railway Company as Agent of the Pondicherry Company on an honorarium kept the accounts of the Company at Trichinopoly and after determining the net profits payable to the Pondicherry Company under the agreement and remitting thereout the share of profits to the French Colonial Government, remitted the balance to the Pondicherry Company in London.

HELD, that the Pondicherry Railway Company carried on a business in British India within the meaning of the Income-tax Act and the income derived from working the line was assessable under Sec. 4 (1) of the Act.

HELD, further that the portion of the net profits payable to the French Government under the terms of the concession was not deductible in computing the assessable profits of the Company.

Case [O. P. No. 115 of 1928], stated under section 66 (2) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

CASE.

I have the honour to state the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (2) of the Indian Income-tax Act, 1922.

2. The petitioner, Mr. Percy Rothera, has been assessed to income-tax as the Agent of the Pondicherry Railway Company, Limited, (hereinafter called the Pondicherry Company) which was incorporated in the United Kingdom in the year 1869 under the Companies Acts, 1862 and 1867.

3. By an agreement dated the 8th May 1878, (hereinafter called the Convention) made between the Minister of Marine and the Colonies in the name of

the French Colony of India of the one part, and the Pondicherry Company of the other part, the company obtained a concession to construct and work the line of railway on French territory from the town of Pondicherry to the river Gingee connecting with the South Indian Railway line from Villupuram. The concession was for a term of 99 years. A copy of the Convention is appended Exhibit A* and forms part of the case.

4. By article 6 of the Convention the Company obtained the lands necessary for the railway and a subsidy from the Colonial Government and in return undertook to make over to the Colonial Government during the whole duration of the concession one half of the net profits from the working of the railway.

5. By an agreement dated 25th March 1879, and made between the Pondicherry Company of the one part and the South Indian Railway Company, Limited, (hereinafter called the South Indian Company) of the other part, the South Indian Company undertook to work, manage and maintain the line of railway constructed by the Pondicherry Company (referred to hereunder as the Pondicherry line), under the terms of its Convention with Colonial Government. This agreement was supplemented by a later agreement dated 30th December 1890, a copy of which is appended marked Exhibit B.*

6. By clause 3 of the later agreement the South Indian Company agreed to provide the rolling stock and with its own staff and plant to maintain the Pondicherry line and all the works, buildings and conveniences connected therewith.

7. By clause 4 the South Indian Company agreed to work the Pondicherry line as if it were an integral part of its own undertaking and to pay the gross receipts from the line into such Government Treasuries in India as the Secretary of State for India may prescribe.

8. By clauses 5 and 6 the South Indian Company undertook to pay over to the Pondicherry Company in India every six months in rupees the balance of profits derived from the working of the Pondicherry line arrived at by deducting from the gross receipts the working expenses incurred by the South Indian Company calculated on the same percentages of gross receipts as the traffic on the undertaking of the South Indian Company including therein the Pondicherry line is from time to time worked out.

9. By clause 8 the gross receipts from traffic to, from and over the Pondicherry line from, or to the undertaking of the South Indian Company, or other railways in connection therewith are computed at a mileage rate and divided between the two companies in proportion to the distance, goods and passengers are carried over each line respectively, the Pondicherry line for that purpose being considered as ten miles in length and any part thereof in the same proportion.

10. The Agent of the South Indian Company who is managing its affairs in India keeps accounts at Trichinopoly to show the receipts and expenses of the Pondicherry line and determines the net receipts payable to the Pondicherry Company according to the agreement with that Company.

11. The petitioner, Mr. Percy Rothera, who is the Agent of the South Indian Company is also the Agent of the Pondicherry Company and is addressed by the Secretary of the latter Company in London as such.

12. Mr. Rothera receives at Trichinopoly on behalf of the Pondicherry Company the profits due to it in accordance with the terms of the agreement with the South Indian Company. This will be seen from the correspondence annexed, Exhibits C* and D*. Under instructions from the Board of Directors in London of the Pondicherry Company he remits the share of profits due under the Convention to the Colonial Government at Pondicherry and remits the balance to the Pondicherry Company in London.

13. Mr. Rothera as the Agent of the Pondicherry Company carries on correspondence with the Directors of the Company in London on matters connected with the working of the Convention and the agreement such as alterations in rates of fares, the preparation of the accounts of the Company and the payment of the share of profits due to the French Colonial Government. He receives a honorarium of £21 a year from the Pondicherry Company "for services rendered".

14. The Chief Engineer and the General Traffic Manager of the South Indian Company are also *ex-officio* of the Pondicherry Company and receive an honorarium of £10-10-0 each. The Revenue Accounts of the Pondicherry Company are prepared by the Chief Auditor of the South Indian Company acting as Chief Auditor of the Pondicherry Company.

15. The Pondicherry Company has an office at Trichinopoly with a sign board.

16. During the year of account 1925-26 the total profits received by Mr. Rothera, on behalf of the Pondicherry Company amounted to Rs. 66,535.

17. The Income-tax Officer, Trichinopoly within whose jurisdiction the petitioner resides called on him as the Agent of the Pondicherry Company to make a return of the Company's income in British India. The petitioner protested on the ground that no income accrued to the Pondicherry Company in British India but eventually a return was filed by the Chief Auditor of the Pondicherry Company. The Income-tax Officer assessed the Agent of the Company on the income returned.

18. The petitioner appealed under section 30 to the Assistant Commissioner and contended *inter alia*:—(1) that the Pondicherry Company was not resident in British India, (2) that as the Pondicherry line from which the Company derives its income was entirely within French territory, no business was carried on by the Company in British India and that no income accrued or arose to the Company in British India, (3) that even if the income accrued or arose to the Company in British India the assessment made on Mr. Rothera as Agent was irregular because he was not given an opportunity of being heard as required by section 43 of the Income-tax Act, (4) that as the Company was not a resident of British India it cannot be assessed on the ground of receipt of profits in British India under section 4, and (5) that in any case in assessing the income of the Company that was derived from the Pondicherry line the share of profits payable to the French Colonial Government in accordance with the Convention should be allowed as a deduction.

19. The Assistant Commissioner decided against the petitioner on all the points.

20. The petitioner requires me to state a case to the High Court on certain questions of law. I agree with his contention that the Company is not a

resident of British India and that it can be reached for the purposes of assessment to income-tax only through its Agents in British India. I refer the following questions for the decision of the High Court: (a) Whether the Pondicherry Railway Company, Limited can be made liable to income-tax when the assessment proceedings have been taken in the name of an Agent in British India and the relevant notices were served only on such agent, (b) Whether the Pondicherry Railway Company, Limited which is resident without British India is liable to be assessed to income-tax on the income derived by it from the working of the Pondicherry Railway under section 4 of the Indian Income-tax Act as income accruing, arising or received in British India, (c) Whether the Pondicherry Railway Company Limited carries on business in British India within the meaning of the Income-tax Act, and (d) Whether in any event the income of the said company that is liable to assessment to income-tax is only that portion which is payable to it under the concession between it and the French Colonial Government.

My opinion thereon is as follows:—

Question (a). The contention seems to be that the petitioner cannot be assessed as the Agent of the non-resident person, viz., the Pondicherry Company, as he was not given an opportunity under the proviso to section 43 of being heard as to his liability to be assessed as such agent.

The relevant provisions of the Income-tax Act that have a bearing on this point are sections 40, 42 and 43. Under section 40 an "Agent" of a person residing out of British India who is in receipt on behalf of such non-resident person of any income chargeable under the Act is liable for the tax. That is, if he is really an *Agent* and in receipt of income on behalf of the principal as Mr. Rothera is in this case nothing more is necessary in order to render him liable; the tax is to be levied upon, and recoverable from him under section 40 irrespective of any other provisions in any other section of the Act. Then comes section 42. Under this section any person residing out of British India whose income accrues or arises within British India shall be chargeable to income-tax in the name of the Agent of any such person and such agent shall be deemed to be for all the purposes of the Act the assessee in respect of such income-tax. Section 43 refers to cases where the non-resident person has no agent in British India appointed by himself as such and it is consequently necessary to find a person who could "be deemed to be such agent". If therefore an Income-tax Officer intends to treat any person not strictly answering to the description of "Agent" as the agent of a non-resident, he can do so only by proceeding in accordance with the provisions of that section. Where a non-resident person, as here, has a duly authorised agent or an agent held out or recognised as such—in this case Mr. Percy Rothera is addressed by the Pondicherry Company as its agent and he is held out as such—it is not only unnecessary but also superfluous for the Income-tax Officer to issue a notice to the agent of his intention of treating him as the agent. It follows that the assessment made on the profits and gains of the Pondicherry Company in the name of its agent is valid.

Apart from this, it seems to me that in this case it is unnecessary to resort to the provisions of Chapter V in the Income-tax Act. The Pondicherry Company is a company formed in pursuance of an Act of Parliament and is therefore a "Company" within the meaning of the Indian Income-tax Act—see sub-section (6) of section 2. Under sub-section (1) of section 22 the Principal Officer of a Company is required to submit to the Income-tax Officer a return of the total income of the Company during the previous year. Under sub-section (12) of section 2 "Principal Officer" used with reference to a local

authority or a Company or other public body or association means, (a) the secretary, treasurer, manager or agent of the authority, company, body or association.....". Mr. Percy Rothera, who is the Agent of the Pondicherry Company is therefore the Principal Officer of the company within the meaning of section 2 (12) of the Income-tax Act; and he was therefore bound, even without any requisition from the Income-tax authorities, to make a return and submit to an assessment. The assessment in this case has been made in the name of the Company in the name of its principal officer and there is no question therefore of any need to issue a notice under section 43 of the Income-tax Act.

Question (b). Under section 4 of the Income-tax Act, the Act is made applicable to all "income, profits or gains from whatever source derived, accruing or arising or received in British India." The words "accrue or arise" as used in this connection seem to me to be general words descriptive of a right to receive and in this light the relevant portion of section 4 (1) may be paraphrased by stating that the income, profits or gains to which the Act applies are income, profits or gains received in British India or income, profits or gains which there is a right to receive in British India. According to the agreement between the South Indian Company and the Pondicherry Company the former has contracted to pay the latter, in India, every six months, in rupees, the profits derived by the working of the Pondicherry line arrived at in a certain manner. As the Pondicherry Company has a right to receive such profits in India and they are actually received at Trichinopoly, I am of opinion that income, profits or gains accrue or arise to the Pondicherry Company in British India, or are received by them in British India and they are consequently chargeable under section 4. In any case the profits resulting from contracts entered into in British India for the carriage of passengers and goods over the Pondicherry line and which produce income to the Pondicherry Company directly accrue or arise in British India and are therefore chargeable under section 4.

Question (c). According to the terms of the agreement between the Pondicherry Company and the South Indian Company the latter has undertaken to work, manage and maintain the line of railway constructed by the Pondicherry Company as if it were an integral part of its undertaking, to pay the gross receipts from that line into such Government Treasuries in India as the Secretary of State for India may prescribe and to pay to the Pondicherry Company in India in rupees the balance of profits derived from the working of the Pondicherry line. In the course of its undertaking the South Indian Company enters into contracts in British India for the carriage of goods and passengers over the Pondicherry line. The business in question in cases like the present ordinarily consists in making contracts for the carriage of goods and passengers and as in this case such contracts are entered into by the South Indian Company as the agents of the Pondicherry Company in British India I am of opinion that the Pondicherry Company is carrying on business in British India.

Question (d). Under Article 1 of the Convention the Pondicherry Company obtained from the French Colonial Government the right to construct and work the *line of railway* called the Pondicherry line and under Article 6 of the Convention the Pondicherry Company undertook on its part "to make over to the Colonial Government during the whole duration of the concession one half of the net profits" (derived by it from the working of the railways). From the facts given above it appears to me that the whole net profit is profit of the Company and assessable in its hands, and no claim has been made in respect of this payment to any deduction under section 10 of the Act. The contention

appears to be that the Company is in the position of a partner with the Colonial Government and is only entitled to a partner's share of the profits. The terms of the Convention—Exhibit A—do not in my opinion support this view.

Nugent Grant, for the Assesseees.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

THE CHIEF JUSTICE:—The Pondicherry Railway Company, Limited was incorporated in England under the Companies Acts in the year 1869. In the year 1878 the Pondicherry Company obtained a concession to construct and work a line of railway in French Territory from Pondicherry to the frontier where it would connect with the South Indian Railway line in Villupuram, the concession to last for 99 years. By article 5 the Pondicherry Railway Co., was empowered "to enter into such contracts as they may deem advisable with the South Indian Railway Company or with any other company either for the working or the maintenance of the line now conceded" and the French Colonial Government gave a subsidy to the Pondicherry Railway Company of about a million and a quarter francs which was obviously intended to cover the probable cost of the construction of the line. There is no question but that the object of the line was to provide a feeder connecting Pondicherry with the South Indian Railway and it is quite clear that the South Indian Railway Company was intended to undertake the whole of the working of the line. The Agent of the South Indian Railway Company became automatically the Agent of the Pondicherry Railway Company and so with the Chief Engineer and Traffic Manager of the S. I. R. Co. In return for the concession and the subsidy the Pondicherry Railway Company was to make over to the French Government during the duration of the concession one half of the net annual profits derived from working the line.

The Pondicherry Railway Company has a registered office in London with a Secretary, and a Board of Directors and there is no doubt that, within the limits of the concession and the agreement between the South Indian Railway Company and the Pondicherry Railway Company to which I will come later, the control of the Company was centred in the Board of Directors in London which would bring it within the doctrine of *San Paolo Railway Company v. Carter*(1), There a railway was entirely worked and run in Brazil. I need not quote the various expressions used by the learned Lords in that case. Perhaps I may sum them up in these words of Lord Halsbury's:—"There is another sense in which the conduct and management, the head and brain of the trading adventure are situated in a place different from that in which the corporeal subjects of trading are to be found", and their Lordships accordingly held that, though all the physical operations relating to the carrying trade took place in Brazil, the head and brain of the adventure was really situated in London and therefore they were subject to tax in England. I make no doubt but that the Pondicherry Railway Company is liable to taxation in England where its board of management is situated. It is also, of course, subject to what is the equivalent of a heavy tax by its obligation to pay half of its net profits over to the French Colonial Government. The question raised here is whether it is also liable to tax in British India.

After the *San Paolo* case it is not, I think, open to argue that any part of the brain of this Company is to be found in British India merely because

(1) 8 Tax Cas. 407; (1896) A. C. 51.

Mr. Rothera, the Agent and other high executive officers of the Company reside there. Nothing can be clearer than the language of Lord Watson at page 41: "Apart from the authority, express or implied which they have from the directors, neither the Superintendent nor any other servant of the company has any power to act in the carrying on of its trade. They are in no sense traders; they are merely servants and in that capacity are remunerated for the services which they are employed to perform. The profits of the undertaking, although they are received by these servants, do not belong to them, and are not in their disposal, their only duty, unless otherwise directed by the Company, being to transmit them to London; and the company here is the sole judge whether they ought or ought not to be distributed among its members".

The first part of what I have quoted makes it to my mind impossible to argue that the mere fact that an important control over the working of the Company is exercised from Trichinopoly which is the head-quarters in British India of the South Indian Railway Company will of itself make the Pondicherry Railway Company liable for taxation here. But two other grounds were put forward on behalf of the Crown. A very large number of cases were cited before us. I only propose to refer to those decisions which seem to me to have the most direct bearing on the matter before us and not to attempt an extensive review of all the authorities. So far as this country is concerned, our function on a case stated is primarily advisory, and such a review of the authorities would not be of assistance to the Commissioner of Income-tax. Whether or no this case can go to the Privy Council, we have not been informed but, if it did, I do not think that, were an Indian Judge to review the authorities at length, his labours would be likely to be of great assistance to their Lordships of the Privy Council. Two other points were taken for the Crown as I said before and I will examine them briefly. In the first place it is argued that, because the South Indian Railway Company, say in Madras, issued through tickets and way bills, that would show that the Pondicherry Railway Company by virtue of the issue of such through tickets and through waybills were carrying on business in British India through the South Indian Railway Company as their agents. Such a view as that of the issue of through waybills and tickets has been negatived for a very long period in the English Courts and, indeed, if one acceded to that principle, one does not know where it would end. You can get in London a through ticket to almost any part of the Continent taking the passenger or the goods over, I know not, how many lines. To say that every company over whose line the ticket was valid was trading in Great Britain would obviously lead to an impossible state of affairs. It was said that there was something in the agreement between the South Indian Railway Company and the Pondicherry Railway Company which invested their relations with the further incident that each railway company was to be the general agent of the other so as to make the Pondicherry Railway Company carry on business in British India through the South Indian Railway Company and I suppose to make the South Indian Railway Company by virtue of through tickets and waybills issued in French Territory to carry on business in French territory. I have read the agreement with great care and I can only say that I can find nothing to warrant any such construction.

Now I come to the main contention for the Crown and I had better begin by stating the course of business on which it is based. What I may call the net profits of the Pondicherry Railway Company after deductions for working expenses, payments to the French Colonial Government and so forth are handed over by the Pondicherry Railway Company from Pondicherry to Mr. Rothera as its agent, he residing in Trichinopoly. It is quite likely that as the servant of the London Directors of the Pondicherry Railway Company, he scrutinises those

accounts and may possibly raise questions about them. He then, having settled the net amount of profits due to the Directors on behalf of the share-holders in England, remits the amount by draft on a London Bank. It is said that this course of business involves the proposition that those net profits must be considered as accruing or arising without British India to a person resident in British India within section 4 (2) of the Act and therefore are received in or brought into British India and must be deemed to have accrued or arisen in British India as the profits and gains of the year in which they are so received or brought. The argument, as I follow it, is that the Pondicherry Railway Company must be deemed to be residing in British India from the fact that their Agent Mr. Rothera resides in British India and that the Pondicherry Railway Company remits funds to him there and that therefore such funds accrue in British India. The unquestionable fact, of course, is that, so far as the remission of the profits goes, Mr. Rothera is a mere post office to convey the Pondicherry earnings to London and not a penny of those funds can be touched or distributed in British India without a gross breach of duty.

I may point out that there are two cases in England where a payment to an agent in England was not held to establish that the agent carried on business in England. One is the well known case of *Grainger v. Gough*(1), where Roederer's London agents, Grainger & Son, received the purchase price of champagne bought by customers in England and transmitted it into France. It was held that, as the operative part of the business was transacted by Roederer direct in France with his English customers and Grainger & Son had no authority to enter into any binding contract on Roederer's behalf, the mere fact that they were used as a convenient channel for collecting and transmitting monies made no difference. To the same effect is *Smidth v. Greenwood*(2). Mr. Patanjali Sastri answers that by a bold proposition that these cases would have been decided differently under the Indian Act on the ground that in England the sole test is carrying on business whereas here the test is the accrual of profits in British India. To my mind, to say that, because for convenience the profits are sent—I suppose by draft—to Mr. Rothera to forward to the directors in London, the profits are to be deemed to have accrued in British India is so technical and unreasonable that it cannot be accepted. Granted the validity of the distinction between carrying on business and having profits accrued to you, I nevertheless think that the analogy of the principle laid down in *Grainger v. Gough*(1), is wholly applicable and that no profits accrued in British India to the Pondicherry Railway Company. It seems to me that it would be just as reasonable to hold that if the Agent of the Pondicherry Railway Company whose business it is to transmit funds to the Company in London ordinarily resided in Pondicherry and received the funds there but was on a temporary visit for business purposes to Madras or Bombay or Calcutta and had the draft forwarded there for him to transmit through a Bank to London, such transmission would involve the proposition that there was an accrual of profits to the Pondicherry Railway Company in British India.

It was at one time suggested that it might be argued that the Pondicherry Railway Company were to be regarded as a mere part of the South Indian Railway. That argument was dropped and I need say no more about it. Here are two distinct statutory corporate bodies, and if they choose to work together for their mutual benefit, that can have no bearing on their respective liabilities. In

(1) 3 Tax Cas 462; (1896) A. C. 825.

(2) 8 Tax Cas. 193; (1921) 3 K. B. 585.

my opinion the assessee is entitled to succeed on this reference and I would answer the questions propounded as follows:—They are four in number (a), (b), (c), and (d). With regard to (a) it was not argued and I do not think it would be arguable on the part of the assessee. It is purely technical and goes to a point of procedure with which we are not now concerned. Questions (b) and (c) which raise the two main points in this case should in my opinion be answered in the negative. If we decide in favour of the assessee railway company on (b) and (c), question (d) does not arise.

As my learned brothers take the opposite view, the order as to (a), (b) and (c) will be as proposed by Odgers, J. That being so, we heard the parties on point (d). It is apparent to us all, that in that view the question of deduction is completely covered by the decision. This was income and had clearly accrued in its entirety to Mr. Rothera in his capacity of Agent of the Pondicherry Railway Company in British India. The answer to this question also must be in favour of the Crown.

ODGERS, J.:—This is a reference to the High Court under section 66 (2) of the Income-tax Act and the following questions have been referred:—(a) Whether the Pondicherry Railway Company, Limited, can be made liable to income-tax when the assessment proceedings have been taken in the name of an Agent in British India and the relevant notices were served only on such agent, (b) Whether the Pondicherry Railway Company, Limited, which is resident without British India is liable to be assessed to income-tax on the income derived by it from the working of the Pondicherry Railway under section 4 of the Indian Income-tax Act as income accruing or arising or received in British India, (c) Whether the Pondicherry Railway Company, Limited, carries on business in British India within the meaning of the Income-tax Act, and (d) Whether in any event the income of the said Company that is liable to assessment to income-tax is only that portion which is payable to it under the concession between it and the French Colonial Government.

The important questions are (b) and (c). The question of allocation we expressly reserved to be dealt with hereafter; this forms the subject of question (d). The Commissioner was of opinion that the Pondicherry Railway Company, was chargeable under (a), (b) and (c) and that under (d) the whole net profit of the Company was liable without deduction. The contentions for the Crown are:—(1) that the income is income accruing or arising in British India, (2) that the Pondicherry Railway Company carries on business in British India through the South Indian Railway Company, (3) that the net profits are payable in India in rupees to the Pondicherry Railway Company or its agent or representative Mr. Rothera and (4) that the profits are paid and received at Trichinopoly by Mr. Rothera in different capacities. All these contentions are traversed by the Railway Company and they further say that, as Mr. Rothera is not a principal agent of the Pondicherry Company, direct assessment to income-tax is irregular.

The Pondicherry Railway Company was constructed under a convention with the French Government of the year 1878 which was to last 99 years. *Inter alia*, the Company, in consideration of the concession granted to it and the subsidy of one and one fourth million francs (roughly) paid to the Company for the construction of the railway, undertook to pay to the French Colonial Government one half of the net profits. The convention and the specification are fully set out in the case and need not at present be referred to in detail. By Ex. B, dated 30th December 1890, an agreement was entered into between the South Indian Railway Company and the Pondicherry Company whereby

the South Indian Company undertook to work the Pondicherry Railway and to provide rolling stock, staff, plant and maintenance. All works required for the accommodation and extension of the traffic were to be constructed at the cost of the Pondicherry Company to the satisfaction of the Engineer in Chief for the time being of the South Indian Company. If the Pondicherry Company did not carry out such works they were to be carried out by the South Indian Company at the cost of the Pondicherry Company. Further the Pondicherry line was to be worked by the South Indian Company as if it were an integral part of their undertaking. The gross receipts are from time to time to be paid into such Government Treasury in India as the Secretary of State may prescribe. The working expenses are to be deducted in the same percentage as from the earnings of the South Indian Company. When the balance of net profit is ascertained, subject to the sanction of the Secretary of State and the provision by him of such moneys as may be necessary for the purpose, it shall be paid over every six months by the South Indian Company to the Pondicherry Company in India in rupees. Further the gross receipts over the two lines are to be computed at a mileage rate and divided between the two companies in proportion to the distance goods and passengers are carried over each line respectively, the Pondicherry line for this purpose being considered as ten miles in length and any part thereof in the same proportion. We have in Exs. VI and C communications between the Secretary of the Pondicherry Company in England and the Agent in this country, who is styled Agent, Pondicherry Railway Company Limited, Trichinopoly, one Mr. Baresford Scott, who, as is well known, was the Agent of the South Indian Company. The letter encloses a statement of the expenses of administration in England amounting to £1595. These figures are furnished to enable Mr. Scott to prepare the revenue account showing the net profit to be divided between the Company and the French authorities. Mr. Scott is then requested to remit the balance due to the Pondicherry Company by draft to London. Ex. D, a letter from Mr. Scott, who signs as Agent to the Pondicherry Railway Company Limited, London, sets out that a cheque for Rs. 12,000 and odd has been sent to the French authorities on account of the moiety of net earnings of the Pondicherry Railway for the year 1922-1923 and that a draft for £1237 was at the same time sent to England representing the Company's share of profits. We know that the Agent of the South Indian Company receives an honorarium of £21 per annum from the Pondicherry Company and similar honoraria of £10-10-0 each are paid to the Chief Engineer and the General Traffic Manager of the South Indian Company.

Now it is said that the residence of the Company is in London where the office and the Board of Directors are situate, that there is the seat of control and the profitable operations are solely carried on in French territory where the profits are all earned. In this view what happens at Trichinopoly is merely the despatch of a demand draft twice a year by Mr. Scott to the Board in London. The office of the Pondicherry Company is in the same building as that of the South Indian Company in London, the Secretary is the same and two of the Directors of the South Indian Company are Directors of the Pondicherry Company. It seems to me that what happens in Trichinopoly may have a very important bearing on the decision of this case. As a matter of fact, although the profits are earned in French territory, they are receivable in and are actually paid under the agreement referred to above in British India and moreover they are calculated not in London but in Trichinopoly as appears to be abundantly established by Ex. C, where we have the amount of the London expenses sent out to the Agent, South Indian Company, in order that profits should be arrived at there.

It has often been pointed out that the Indian Act section 4 (1), differs very materially from the English Act, Schedules (C), (D) (1) where importance

is attached to persons residing in the United Kingdom, whereas under section 4 (1) the Indian Act applies to all income, profits or gains accruing, arising or received in British India. This difference has been pointed out in several cases, as for instance, in *Secretary to Board of Revenue v. Ramanathan Chetty*(1), where Abdur Rahim, Offg. C. J., says:—"In the English statute the place of residence of a person is a basis of assessment but is not so as pointed out above in Act VII of 1918". The difference is also very distinctly shown in *Rogers Pyatt Shellac & Co. v. Secretary of State for India*(2). That was a case of factory in the United Provinces which bought goods in London for sale in the United States of America. They had also an office in Calcutta. In the factory the goods were worked up into a form suitable for export to America and it was held that the company was not exempt from income-tax. The importance of the case is in the *dicta* of the learned Judges of the difference between the English and the Indian Law. At page 370, Chatterjee, J. says—"The English Income-tax Acts lay down a territorial limit," and further at page 372, "In order to determine whether the income is taxable under the Act, the place at which it has accrued, or has arisen or has been received has got to be ascertained. The section ignores the person and only takes into account the place where the income accrues, arises or is received". Again "if the income is received in British India no matter wherever it may have arisen or accrued, that is to say, if it is received by a resident in British India from sources that lie outside, it is taxable". Mr. Justice Mukerji quoting from *Colquhoun v. Brooks*(3), says "Lord Herschell observed—"The Income-tax Acts themselves impose a territorial limit either that from which the taxable income is derived must be situate in the United Kingdom, or the person whose income is to be taxed must be resident." This fundamental principle of the English statutes does not appear in the Act VII of 1918 or Act XI of 1922. The question of residence does not arise, nor any territorial limits are recognised by the charging sections of the said Acts." Further at page 375, "In the Indian Statute the question where the trade is exercised does not come in at all". The learned Judges dissent from the case in *Board of Revenue v. Madras Export Co.*(4), on the ground that our Court did not recognise the change in the later Act from the earlier one. Mukerji, J., at page 376 says,—"The Indian Law does not proceed upon the basis of such a condition but upon the taxability of the income regarded from the point of view of the place where it accrues, arises or is received under the Act".

In *Sulley v. Attorney-General*(5) it was pointed out that a man exercises his trade where his profits come home to him. So the test of where a trade is carried on has been applied in more than one English case; for instance in *Smidth v. Greenwood*(6), Atkin, L. J., said that the place where the trade is carried on is important but not decisive. The proper test is, "where do the operations take place from which the profit in substance arises". In *Grainger v. Gough*(7), the principal test was stated to be where the contracts are made, for it is there that the business is carried on, this being a question of fact—see 1896. A.C. 31. In the Broken Hill case, *Commissioners of Taxation v. Kirk*(8), decided by the Privy Council, profits were partly derived from the treatment and extraction of the ore in New South Wales. The company was held assessable in New South Wales, it being a question of fact as to whether any part of the profits was earned in that Colony, the finding being that it was. In a very

(1) 1 I. T. C. 37; 43 Mad. 75

(3) 2 Tax Cas. 490; (1889) 14 App. Cas. 493.

(4) 1 I. T. C. 194; 46 Mad. 360.

(6) 8 Tax Cas. 193.

(8) (1900) A. C. 588

(2) I. T. C. 363; 52 Cal. 1.

(5) 2 Tax Cas. 149.

(7) 3 Tax Cas. 462.

recent case *Latham v. Muller & Co., (London), Ltd.*(1), it was held that the shipping company did exercise a trade in England and did not merely trade with England, as a very considerable portion of the carrying voyage was executed in English territorial waters, the shipment, delivery of goods and contracts for carriage binding the shipping companies are made in the United Kingdom and freight received therein. That, in the opinion of the learned Judges, has constituted the exercise of a trade in the United Kingdom.

However these cases have really very little to do with the point that has to be decided in the present case because, as already pointed out, the words of the charging section in the Indian Act are totally different from the words in the English Act. So, as pointed out in *In re Aurangabad Mills*(2), under the English law, the Hyderabad Company would have been taxed as the test is there, where do they carry on business, and not where are the profits derived. So in *Secretary to Board of Revenue v. Ripon Press Sugar Mills Co., Ltd.*(3), in which *In re Aurangabad Mills*(2) was followed the only money received in British India was for office expenses and for the payment of dividends to some of the shareholders who preferred to be paid there.

Much discussion has taken place as to the meaning of the words "arises or accrues". In *Colquhoun v. Brooks*(4), the words are construed as meaning a right to receive (Per Fry, L. J., page 59). As I have previously pointed out the real point under this part of the case is what happened in Trichinopoly. As I read the agreement the two Companies are practically one undertaking. No separate books are maintained in Trichinopoly for the Pondicherry Company, but the two undertakings are treated as one. As the Pondicherry Company has to pay half its gross profits to the French Colonial Government it is necessary to arrive at a figure which is called the net profits of the Pondicherry Company. This is determined in Pondicherry after a comparison of the profits of the South Indian Company taken together with those of the Pondicherry Company which as stated are not kept separate. The whole of this work is done in Trichinopoly. The whole of the profits derived from the Pondicherry Company, though no doubt earned in French soil is treated as part of the income of the South Indian Railway Company and are notionally divided in accordance with the rough and ready method contained in paragraph 8 of the agreement for the purpose really of arriving at the sum payable to French Government and I take it that this is the real reason why the two Companies are technically kept distinct. The Agent of the South Indian Railway is the Agent of the Pondicherry Railway, the officers of the South Indian Railway have the entire and complete control of the Pondicherry line and the working of the trains over it. The money derived therefrom is paid in accordance with paragraphs 4, and 6 of the agreement and it is undoubtedly paid in British India. I therefore think that the profits do arise in Trichinopoly and are assessable there under the Indian Act.

It is secondly contended that the South Indian Company is the Agent of the Pondicherry Company. Under the terms of the agreement, I think this is so. But it is contended that under the through-ticket arrangements by which you can take, say a ticket at Egmore for Pondicherry, the agency is further established and the Pondicherry Company thus carries on business in British India. It is said that the issue of through tickets cannot in all instances have

(1) 13 Tax. Cas. 126 ; (1928) A. C. 34.

(2) 1 I. T. C. 116 ; 45 Bom. 1286.

(3) 1 I. T. C. 202 ; 46 Mad. 706.

(4) 2 Tax. Cas. 490 ; (1888) 21 Q. B. D. 52.

this effect. If I take a through ticket from London to Rome, for instance, it would be obviously ridiculous to hold that the Italian Railway Company is carrying on business in England by reason only of the issue of that through ticket. Through tickets of that sort are no doubt surrounded with various exceptions and special contracts with which we have nothing to do here. Several cases have been quoted to show, for instance, that only the first company, i.e., in the case of through tickets from Madras to Pondicherry the South Indian Company would be liable. The cases are all old ones as, for instance, 8 M. & W. 421, a case of 1841, where it was held to be a question for the jury as to whether the defendant company undertook to convey the parcel beyond Preston. The case does not say that the other company, i.e., the carrier beyond Preston would not be liable. In 7 H. L. 194, a case of 1859, the contract was held to be with the first company (G. W. R.), alone and subject to its conditions. The whole case turned on the construction of the 10th condition. On the other hand, in the well known case of *Foulkes v. Metropolitan District Railway Company*(1), through tickets there were held to be issued as agents or partners by the South Western Railway and the defendants were held liable certainly in tort and, according to all the judges, in contract as well. So in *Thomas v. Rhymney Railway Company*(2), the defendants were held liable though the accident was due to the negligence of the servants of the T. V. Company and it was held that the contract was the same whether the journey was entirely over their own line or partly over the line of another company under an agreement to share profits or simply under the running powers. One case was quoted by Mr. Alladi Krishnaswami Iyer in reply 11 Ch. D. 625, where it was held that on the construction of the Act of Parliament and the working agreement the L. C. & D. Railway Company were entitled to exclusive possession and right of maintenance and that the erection of steps by the Sevenoakes Company was a work of maintenance which that company was not entitled to carry out. The arrangement would appear to be very similar to the arrangement here where as pointed out above the entire maintenance of the Pondicherry line is put in the hands of the South Indian Railway Company.

Mr. Krishnaswami Iyer further attempted to explain the relationship between the two companies as that of lessor and lessee on the ground that the Pondicherry Company never intervenes as a principal and has handed itself over to the South Indian Company who practically acts as its principal. There is no evidence here of any such relationship of lessor and lessee and no documents or evidence before us to enable us to say that such relationship exists. I therefore think that on the construction of the agreement as well as on the legal relations established by the issue of through tickets and waybills that it is undoubted that the South Indian Railway Company is the agent of the Pondicherry Company in British India. The Pondicherry Company, as so often pointed out, has really no separate existence. It carries on the whole of its operations through the agency of the South Indian Railway Company. I think therefore that the questions referred to us (b) and (c) must be answered in the affirmative. Question (a) was not seriously argued and I do not think it necessary to return an answer on that.

With regard to (d) we have reserved the question and if this judgment finds support from either of my learned brothers, the question will no doubt have to be argued before us again on some future occasion.

I have now had the advantage of reading and considering my brother Beasley, J.'s judgment on point (d). I am in complete agreement with it and have

(1) 5 C. P. D. 157.

(2) 6 Q. B. 266.

nothing to add. The assessee will pay Rs. 750 as costs to the Commissioner of Income-tax.

BEASLEY, J.:—The facts have already been fully stated in the answer to this reference of my learned brother Odgers, J., which I have had the advantage of reading and with whose conclusions I entirely agree; and I therefore do not propose to re-state those facts. In my view, the answer to this reference must be in favour of the Commissioner of Income-tax by reason of the wording of section 4 (1) of the Indian Income-tax Act which is as follows: "Save as hereinafter provided, this Act shall apply to all income, profits or gains, as described or comprised in section 6, from whatever source derived, accruing, or arising, or received in British India or deemed under the provisions of this Act to accrue, or arise, or to be received in British India." Therefore all income derived or accruing or arising in British India is subject to taxation and in this respect the charging section of the Indian Income-tax Act of 1922, differs very materially from the English Act. Under the English Income-tax Act an important test is where the business or trade of the assessee is exercised, or where the contracts are made, or where the place of management and control is situate. It was argued for the assessee that the well known case of *Grainger & Son v. Gough*(1), *Sulley v. Attorney-General*(2), *San Paulo Railway Co. v. Carter*(3), and *Smith v. Greenwood*(4), are authorities strongly in their favour, because it is contended that following those authorities the place in which the management and control of a business is centred is the place where the trade is exercised or business carried on and that as the offices of the Pondicherry Railway Co., are in London where its Board of Directors meets that is the place where the business of the Pondicherry Railway Company is carried on.

If the words in the Indian Income-tax Act were the same as those in the English Income-tax Act, then the cases relied upon by the assessee would be conclusive of this matter, but they are not the same, and the important difference has been pointed out by the Indian Courts. In *In re The Aurangabad Mills, Limited*(5), the words of section 3 (1) of the Indian Income-tax Act of 1918 were considered. They are "Save as herein-after provided, this Act shall apply to all income from whatever source it is derived, if it accrues or arises or is received in British India, or is, under the provisions of this Act, deemed to accrue or arise or to be received in British India." These words are practically identical with those of section 4 (1) of the Indian Income-tax Act of 1922. In that case all the profits of the company were earned in His Exalted Highness the Nizam's territories but the company had an office in Bombay where the Directors of the company managed the business and it was sought to tax the company in India on the latter account; and the English cases were relied upon by the Revenue authority but it was held by Macleod, C. J., and Shah, J., that the income was not taxable. Macleod, C. J., at page 119, states: "Undoubtedly if the English law had applied to this case the profits could have been taxed. But under the English law, the test is, where the company carry on business, and not, where are the profits derived. And the Chief Revenue authority has erred in thinking that the English cases he has cited are applicable to this case, for, in England a company is said to carry on its business where it has its registered office irrespective of where its profits are derived".

This case was followed in *The Secretary, Board of Revenue v. Ripon Press and Sugar Mills Company, Limited*(6) a reference to a Full

(1) 3 Tax Cas. 462.

(3) 3 Tax Cas. 407.

(5) 1 I. T. C. 116.

(2) 2 Tax Cas. 149.

(4) 8 Tax Cas. 193

(6) 1 I. T. C. 202

Bench consisting of Sir Walter Schwabe, C. J., Oldfield and Coutts Trotter, J., If the test in that case had been where the company exercised its trade or carried on its business as it is under the English Income-tax Act, the decision would probably have been that the assessee—company was liable to taxation, following the English decision in the *San Paulo Railway* case. But as the test is where the profits and gains accrue, the decision following that of the Bombay High Court, in the *Aurangabad Mills* case, was the other way. Another important case is *Re Rogers Pyatt Shellac & Co. v. Secretary of State for India*(1). In that case a company, incorporated in the United States of America and having its head office in New York and branch office, agencies and factories in Calcutta, London, &c., which purchases goods in India for sale in the open market in America or for another company in America (the commission for the purchase for the company being paid in America) and which has also a factory in the United Provinces, where raw produce is bought locally and is worked up into a form suitable for export to America, is not exempt from assessment to income-tax or super-tax in India. In this case *Sulley v. Attorney-General, Grainger & Son v. Gough* and *Smidth & Co. v. Greenwood* were distinguished. It was argued for the Secretary of State that the English decisions would hardly be of any assistance to the Court for the reason that the scheme of the English Acts was entirely different from that of the Indian Acts. The English Act imposes a territorial limit with regard to income chargeable to income-tax, either that from which the taxable income is derived must be situate in the United Kingdom, or the person taxed must be resident there. It was contended that on the other hand the Indian Acts of 1918 and 1922 make the Acts applicable to all income from whatever source it is derived or arises or is received in British India. Chatterjee, J., after referring to *Grainger & Son v. Gough*(2), and *Sulley v. Attorney-General*(3), on page 366 states. "It will be seen that under the English Acts it is essential that the profits should arise from the exercise of the trade within the United Kingdom. In the Indian Acts (VII of 1918 and XI of 1922) however, in the case of any person residing out of British India all profits or gains accruing or arising to such person whether directly or indirectly through or from any business connection in British India shall be deemed to be income accruing or arising within British India. There is no such provision in the English Acts, and that distinguishes the English Acts, and the cases decided thereunder from the Indian Acts."

What happens in Trichinopoly? The whole of the profits derived from the Pondicherry Company, though earned in French territory, are treated as part of the income of the South Indian Railway Company and divided in accordance with paragraph 8 of the agreement. The Agent of the South Indian Railway Company is the Agent of the Pondicherry Railway Company and the offices of the South Indian Railway Company have the entire management of the Pondicherry line. The money obtained from the working of the Pondicherry line is paid in British India, and a large part of the revenue of the Pondicherry Railway is collected in India by the officials of the South Indian Railway Company; for example, if a passenger travels from Madras to Pondicherry or any station within the French territory to which the Pondicherry Railway runs he takes his ticket at Madras and pays for it here. So much of the fare as is apportionable to the Pondicherry Railway Company is collected here in British India. It never goes to Pondicherry at all and is eventually sent by Mr. Rothera, the Agent of the Pondicherry Railway Company, to London. In my view, the profits and gains of the Pondicherry Railway Company accrued in British India

(1) 1 I. T. C. 363.

(2) 3 Tax Cas. 462 ; (1896) A. C. 325.

(3) 2 Tax Cas. 149.

and I agree with my learned brother Odgers, J., that the Pondicherry Railway is on that account liable to be taxed. I also agree with my learned brother that the Pondicherry Railway Company carries on business in British India within the meaning of the Indian Income-tax Act for the reasons he has given.

The only question remaining to be decided is whether the sum payable by the Pondicherry Railway Company to the French Colonial Government should be allowed as a deduction in computing the assessable profits and gains of the business.

Under Art. 6 of the agreement of 1878 between the French Colonial Government of India and the Pondicherry Railway Company the latter undertakes to make over to the Colonial Government during the duration of the concession one half of the net profits of the concern. The Pondicherry Railway Company contend that this amount is not assessable to income-tax because (1) it is not income at all, or (2) it can be deducted under section 10 (2) of the Indian Income-tax Act as an allowance. With regard to the former contention, in my view, this is clearly income. The payment is made out of the net profits of the business and the profits of the business represent the taxable income of an assessee and we have already held that this is income accruing to the Pondicherry Railway Company in British India. With regard to the latter contention the only part of section 10 of the Act which, it is suggested, can possibly apply is sub-section 2 (ix), namely, "any expenditure not being in the nature of capital expenditure incurred solely for the purpose of earning such profits or gains". It is argued that this sum was agreed to be paid to the French Colonial Government in order to get the permission to construct and work the railway. No doubt it is an yearly payment to the French Colonial Government for the concession, but is payable out of profits. If there are no profits then no payment is made. The payment is entirely dependent upon the earning of profits and, in my view, the payment is a distribution of those profits and is not an allowance deductible from those profits.

I would therefore answer this question in the negative.

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